University of Alberta

Contextualizing the Harmonization of Accounting Standards for Foreign Currency Translation

By

Barbara Mary Wheeling ©

A thesis submitted to the Faculty of Graduate Studies and Research in partial fulfillment of the requirements for the degree of Doctor of Philosophy in Accounting

Faculty of Business

Edmonton, Alberta

Fall 1999

National Library of Canada
Acquisitions and Bibliographic Services
395 Wellington Street
Ottawa ON K1A 0N4
Canada

Bibliothèque nationale du Canada
Acquisitions et services bibliographiques
395, rue Wellington
Ottawa ON K1A 0N4
Canada

Your file Votre référence

Our file Notre référence

The author has granted a non-exclusive licence allowing the National Library of Canada to reproduce, loan, distribute or sell copies of this thesis in microform, paper or electronic formats.

The author retains ownership of the copyright in this thesis. Neither the thesis nor substantial extracts from it may be printed or otherwise reproduced without the author's permission.

L'auteur a accordé une licence non exclusive permettant à la Bibliothèque nationale du Canada de reproduire, prêter, distribuer ou vendre des copies de cette thèse sous la forme de microfiche/film, de reproduction sur papier ou sur format électronique.

L'auteur conserve la propriété du droit d'auteur qui protège cette thèse. Ni la thèse ni des extraits substantiels de celle-ci ne doivent être imprimés ou autrement reproduits sans son autorisation.

0-612-46943-3

Canada

University of Alberta

Library Release Form

Name of author: Barbara Mary Wheeling

Title of Thesis: Contextualizing the Harmonization of Accounting Standards for Foreign Currency Translation

Degree: Doctor of Philosophy

Year this Degree Granted: 1999

Permission is hereby granted to the University of Alberta Library to reproduce single copies of this thesis and to lend or sell such copies for private, scholarly, or scientific research purposes only.

The author reserves all other publication and other rights in association with the copyright in the thesis, and except as hereinbefore provided, neither the thesis nor any substantial portion thereof may be printed or otherwise reproduced in any material form whatever without the author's prior written permission.

Barbara Mary Wheeling

992 S. 3500 E., New Harmony, Utah 84757

20 August 1999

University of Alberta

Faculty of Graduate Studies and Research

The undersigned certify that they have read, and recommend to the Faculty of Graduate Studies and Research for acceptance, a thesis entitled Contextualizing the Harmonization of Accounting Standards for Foreign Currency Translation submitted by Barbara Mary Wheeling in partial fulfillment of the requirements for the degree of Doctor of Philosophy in Accounting.

David J. Cooper

Jim Gaa

Gordon Laxer

Yves Gendron

Alan Richardson

19 August 1999

ABSTRACT

The one-dimensional view of power is evident in the development of foreign currency accounting standards. Particular multinational corporations (MNCs) exhibited the power to exert their influence over the preferences of other MNCs as they sought to influence the deliberations over the specific provisions of the standards. Conflict among the MNCs as they strived to preserve their preferred methods and engage others to adopt or accept those methods is indicative of one entity getting another entity to do what they otherwise would not do. The results of the deliberation over the standards for foreign currency accounting indicate that those MNCs whose preferences for accounting methods and treatments that were adopted by standard-setting bodies were successful in exerting their power to influence others.

By the establishment of networks and enrolling the support of the standard-setting bodies, the MNCs were able to stabilize the relations necessary for exercising their power. The resistance exhibited by the MNCs and other interested parties also contributed to the eventual outcomes in the provisions of the standards.

Consistent with the three-dimensional view of power, the discourse on harmonization influenced standard-setters, MNCs, and other interested parties to not merely develop foreign currency standards but also to harmonize these standards with other countries. Thus, accounting standards for foreign currency are the result of a fabrication process involving networks of alliances used to stabilize relations in order to exert power, the resistances to specific provisions that refabricated the standards, and the power exerted through the discourse on harmonization of accounting rules to influence the outcomes of deliberations over foreign currency accounting standards.

TABLE OF CONTENTS

LIST OF TABLES

LIST OF ABBREVIATIONS

Chapter

1. Introduction 1

Motivation for the Study 4
Foreign Currency Standards and Issues in International Accounting Harmonization 11
The Political and Economic Context of Foreign Currency Accounting 20
Conclusion 35

2. The Developments in Accounting for Foreign Currency Translation 39

Method 42
A Comparison of Methods and Pronouncements on Foreign Currency Accounting 50
Currency Fluctuations 56
Conclusion 70

3. A Comparative History of Accounting for Foreign Currency Translation 74

Current Practice Argument 81
Accounting Principles Argument 91
Lobbying Efforts 109
Tax Considerations 122
Conclusion 136

4. The Role of Power in Setting Foreign Currency Standards 142

Theories of Power 153
The Role of MNCs in Developing Foreign Currency Accounting 164
Efforts to Harmonize Standards on Foreign Currency Accounting 195
Conclusion 215

5. Conclusion 218

BIBLIOGRAPHY 226

APPENDIX I. Mill's Methods 241

TABLE OF CONTENTS (CONT.)

APPENDIX IIA. Exchange Rates, National Currencies Against the United States Dollar.....242

APPENDIX IIB. Effective Exchange Rates, Percentage Changes from 1st Quarter 1970.....243

APPENDIX IIC. Exchange Rates of Major Currencies Against the Dollar.....244

APPENDIX III. Inflation Effects of Translation Methods.....245

APPENDIX IV. Tax Effects of Translation Methods.....247

LIST OF TABLES

Table Page

1. Pronouncements on Accounting for Foreign Currency Translations and Transactions.....72

LIST OF ABBREVIATONS

AARC	*Australian Accounting Research Committee*
AARF	*Australian Accounting Research Foundation*
AAS	*Australian Accounting Standard*
AASB	*Australian Accounting Standards Board*
AASC	*Australian Accounting Standards Committee*
AIA	*American Institute of Accountants*
AICA	*Australian Institute of Chartered Accountants*
AICPA	*American Institute of Certified Public Accountants*
APB	*Accounting Principles Board*
APBO	*Accounting Principles Board Opinion*
APTF	*Accounting Principles Task Force*
AR	*Accounting Recommendation*
ARB	*Accounting Research Bulletin*
ARC	*Accounting Research Committee*
ASA	*Australian Society of Accountants*
ASB	*Accounting Standards Board*
ASC	*Accounting Standards Committee*
ASRB	*Accounting Standards Review Board*
ASRC	*Accounting Standards Review Committee*
ASSC	*Accounting Standards Steering Committee*
Bull.	*Bulletin*
CAP	*Committee on Accounting Principles*
CCAB	*Consultative Committee of Accountancy Bodies*
CICA	*Canadian Institute of Chartered Accountants*
DoT	*Department of Trade*

LIST OF ABBREVIATIONS (CONT.)

E, ED	*Exposure Draft*
EEC	*European Economic Community*
FAS	*Financial Accounting Statement*
FASB	*Financial Accounting Standards Board*
FEI	*Financial Executives Institute*
GAAP	*Generally accepted accounting principles*
GDP	*Gross Domestic Product*
IASC	*International Accounting Standards Committee*
IASs	*International Acccounting Standards*
ICAEW	*Institute of Chartered Accountants in England and Wales*
ICAI	*Institute of Chartered Accountants of India*
IMF	*International Monetary Fund*
INT	*Interpretation*
IOSCO	*International Organization of Securities Commissions*
MNCs	*Multinational corporations*
NAA	*National Association of Accountants*
OECD	*Organization of Economic Development*
OP	*Opinion*
PSASB	*Public Sector Accounting Standards Board*
REV	*Revised*
ROI	*Return on Investment*
SEC	*Securities and Exchange Commission*
SSAP	*Statement of Standard Accounting Practice*
ST, STD	*Standard*
TPA	*Technical Practice Aid*

CHAPTER 1. INTRODUCTION

The purpose of this dissertation is to provide an understanding of the development of foreign currency accounting standards in terms of concepts of power[1] and the role of specific multinational corporations (MNCs) in that process. This dissertation points out how certain conditions present from the early 1970s to the late 1980s that suggest reasons for prescribing one method or another by accounting standard-setters do not fully explain the decisions made by the standard-setting groups as they developed different standards to begin with and later moved towards consensus. It also shows how specific social relations between standard-setting bodies and MNCs demonstrate the role of power in the standard-setting process, specifically how representatives from certain MNCs were placed in strategic positions to influence the outcomes of the standards, and how these relations affected the policy making strategies of the national standard-setting bodies in coping with a new international monetary system and in the movement towards harmonization[2] of these standards.

---

1 Power in this study is based on Luke's three-dimensional view of power. In all three dimensions power is considered relational and involving either overt or covert conflict. (S. Lukes, *Power: A Radical View* (London: Macmillan, 1974)).

2 Harmonization has been viewed as establishing uniformity in accounting rules (Jacob Kraayenhof, "International Challenges for Accounting", *Journal of Accountancy* (January 1960): 34-38) and also as reducing the diversity in accounting rules (Arthur R. Wyatt, "International Accounting Standards and Organizations: Quo Vadis?", in Frederick D. S. Choi, ed., *Handbook of International Accounting* (New York: John Wiley & Sons, 1992)). In this dissertation harmonization is considered the process of achieving a consensus concerning what the accounting rules should be and establishing a set of

This study contributes to the international accounting literature by demonstrating the effects of efforts towards international harmonization on national efforts to develop a standard for foreign currency translation. Current literature describes the outcomes but not the process of harmonization among the standard-setters in US, the UK, Australia, Canada and the International Accounting Standards Committee (IASC),[3] leaving unanswered such questions as why these groups would choose to harmonize.

Examining the nature of developing accounting standards requires building on the conventional, technical descriptions of accounting standard-setting and viewing this process in light of theories of power to understand the complexities involved in determining international standard-setting policy. This study contributes to the critical literature by showing how foreign currency standards are the result of a process involving power and networks of alliance. In this study on foreign currency accounting, this dissertation argues that technical descriptions or conventional comparative studies of the results of standard-setting processes overlook the socio-political nature of international accounting standard-setting. By analysing the historical development of standards for foreign currency translation as a social process within an international context after 1970,

---

standards that reflect that consensus. This definition is more representative of reducing diversity rather than establishing unifomity in accounting rules in that completely uniform standards have not been established but that a degree of reducing the diversity has been agreed upon.

3

Robert J. Kirsch and Dawn Becker-Dermer, "Proposed Revisions of International Accounting Standard No. 21 and their Implications for Translation Accounting in Selected Countries: The US, the UK, Australia, and Canada", *International Journal of Accounting* 30 (1995):1-24. These four countries and the IASC are also known as the G4+1.

this dissertation shows that understanding the processes of accounting standard-setting policy leads not necessarily to the rejection of more technical approaches, but rather an expansion beyond these approaches.

The history of the development of standards for foreign currency accounting suggests that cooperation and mutual consideration among the standard-setting bodies in the US, the UK, Australia, Canada, and the IASC that led to the current level of consensus is a relatively recent occurrence. In the early 1970s various methods of translation and treatments of gains and losses were endorsed by standard-setting bodies in the US, the UK, Australia, and Canada where the debate over translation methods was most prevalent.[4] In view of calls for harmonization in the late 1960s and early 1970s and the beginning of a floating exchange rate system in 1973 that affected all countries simultaneously, why, initially, were different methods of accounting for foreign currency translation endorsed by different standard-setting bodies, and, how, subsequently, did the move toward consensus evolve?

This dissertation addresses only one topic in the field of international accounting standard-setting. Presumably, each topic that concerns accounting standard-setters raises a different set of issues and actors in the process of developing a standard. While the

---

[4] In FAS 8 the US endorsed the temporal method of translation. Later they allowed both the current rate method and the temporal method. Canada endorsed several methods initially, then only the temporal method. Australia and the UK endorsed the current rate method and later the UK endorsed both the temporal method and the current rate method, *before* the US endorsed both methods. The countries were divided in handling gains and losses with the US at first only permitting income statement treatment while most of the other countries permitted some form of deferral.

events and circumstances of developing accounting standards for foreign currency cannot be generalized to other topics, it can reveal some particular insights into who controls that process. Each issue in international harmonization is different, depending on which parties are involved in the process. Unless we delve more deeply into understanding this process and the players involved and consider the role that standard-setting bodies take in the power struggles that ensue, we will continue to place credit or blame on social and political factors that are only partially responsible for these struggles.

The purpose of this chapter is to provide the background in which accounting standards for foreign currency developed. Part I presents the motivation for studying the history of foreign currency accounting. Part II discusses how a study of foreign currency standards has implications for understanding the complexities of international harmonization. Part III describes the political and economic environment leading up to the development of these standards by recounting the events up to and including the dismantling of the fixed-rate exchange system, the developments in international investment and the globalization of business, and the implications these developments had for accounting and accounting standard-setting for foreign currency. Part IV contains concluding remarks on the implications of this study and a brief outline of the remaining chapters.

I. Motivation for the Study

Accounting for foreign currency translation has been viewed primarily as a

controversial technical issue, with the literature in accounting focusing on similarities and differences in technical areas.[5] For example, Kirsch and Becker-Dermer compare and contrast foreign currency standards in English-speaking countries to "discern the degree of harmonization between countries and the IASC and to shed light on the prospects for harmonization in this area in the future."[6] Their analysis attributes consensus to discussion, observation, and imitation on the part of standard-setting bodies while recognizing the many differences that exist among the standards. Although the paper offers an excellent account of the technical details of the foreign currency standards in the English-speaking countries, it merely points out the nature of these differences. There is no empirical evidence or theoretical discussion concerning the development of consensus, nor are there any explanations for the differences. Their conclusion was that the IASC must complete its work on E44 and national accounting bodies must bring their own standards in line with E44. But without an understanding of the complex issues involved in foreign currency and the preferences and actions taken by interested parties, one cannot begin to assess the nature of the difficulties associated with harmonizing such a controversial topic.

Accounting for foreign currency translation has a long history, but we know little about its social roots or the interrelation between the social and the technical. The social

---

5 See Chapter 2 for a more complete literature review on foreign currency standards. For an early review, see C. W. Nobes, "A Review of the Translation Debate", *Accounting and Business Research* (Autumn 1980): 421-431.

6 Kirsch and Becker-Dermer, *ibid.*

refers to the aspects of accounting that reflect social relationships.[7] The technical refers to the perspective of accounting that views it as a set of calculations.[8] Accounting in general has gained in significance in organizations and societies and hence is increasingly seen as more than its technical aspect. The increasing demand for financial information by capital markets, the state, and other entities suggest that accounting standards serve as an influential mechanism for economic and social management, but how they evolved in that way is little understood.[9] No framework exists for analysing the specific case of foreign currency translation practices against the conditions in the socio-economic system or for explaining the social practices that constitute the relationship between MNCs and accounting regulators and how these relationships affect the technical decisions made by standard-setting bodies.

Foreign currency translation is reflective of societal activity and is embedded in relations of power. Foreign currency accounting is a social practice and necessitates a conceptualization of power in that the development of foreign currency accounting standards represents a struggle for legitimation of authority. Technical descriptions of standards for foreign currency accounting do not reflect the implications of the choices made by standard-setting bodies on the structures of contemporary international business.

---

7 Stuart Burchell, Colin Clubb, Anthony Hopwood, John Hughes, and Janine Nahapiet, "The Roles of Accounting in Organizations and Society", *Accounting, Organizations and Society* 5 (1980): 5-27.

8 *Ibid.*

9 *Ibid.*

(1) MNCs as opposed to competitive national firms as dominant players and the various business environments in which they operate, (2) information requirements from many jurisdictions beyond national borders, including investors from foreign countries, governments, and organizations such as the United Nations, and (3) the inherent difficulties associated with movements towards international harmonization of trade and commerce to facilitate capital flows and the implications of these difficulties for employees, communities, regulatory agencies such as standard-setting bodies, the accounting profession, etc. The movement towards harmonization in international accounting raises questions concerning national standard-setting bodies' rights to set standards within their own borders and the rights of MNCs to engage in financial reporting activities that are (or at least perceived to be) conducive to the firm's growth and survival.[10] In view of various interests in accounting information that exist,[11] what do we really know about the process by which standards for foreign currency accounting developed?

This study also points out that one cannot take for granted that a particular standard-setting body made choices based solely on certain socio-economic conditions

---

[10] The development of standards for foreign currency accounting reflects this notion in the criticisms of FAS 8 which resulted in corporate managers having to spend resources to hedge against economic losses from the volatility of earnings due to provisions that required income statement treatment of foreign exchange gains and losses. (See Richard C. Laughlin and Anthony G. Puxty, "Accounting Regulation: An Alternative Perspective", *Journal of Business Finance & Accounting* 10 (1983): 451-479.)

[11] *Ibid.*

that existed in its domain. In discussing the difficulties of harmonizing standards for foreign currency, it is not enough to understand why standard-setters in the UK, for example, initially opposed and later adopted the temporal method that was endorsed in the US. One must understand the reasons why they preferred the current method to fully understand the difficulties associated with arriving at consensus. Technical historical accounts are useful in relating the facts but are inadequate in terms of explaining them. Popular viewpoints emphasize the role of the US SEC or political differences between approaches to standard-setting in countries like the US and Germany in explaining impediments to harmonization. The accounting literature suggests that a number of social, economic, and political factors may be involved.[12] While not wishing to deny the importance of these factors, these views fail to recognize the importance of the roles played by outside entities, such as powerful MNCs with the resources and the interest in becoming involved in accounting standard-setting. The role of MNCs in standard-setting

---

12

These include variations in attitudes concerning the organization and control of society, institutional pressures from capital markets, governments, and banks, and differences in professional and educational standards among accounting professions across countries. (Desmond McComb, "International Accounting Standards and the EEC Harmonization Program: A Conflict of Disparate Objectives", *The International Journal of Accounting Education and Research* (Spring 1982): 35-48.) Other suggested impediments include inconsistencies with national standards, influences of tax laws, influences of company laws, nationalism, differences in user needs, lack of enforcement across international boundaries, concern about the quality and nature of international standards, and the reluctance of national bodies to take required action. (Alister K. Mason, "The Development of International Financial Reporting Standards", *ICRA Occasional Paper No. 17*, (Lancaster, England: International Center for Research in Accounting, University of Lancaster, 1978); Juan M. Rivera, "The Internationalization of Accounting Standards: Past Problems and Current Prospects", *The International Journal of Accounting Education and Research* 24 (1989): 320-341.)

processes is largely underemphasized in accounting literature.

Examining one particular issue of accounting standard-setting, foreign currency accounting in the US , the UK, Australia, Canada, and the IASC, focuses attention on the dynamic interaction of national and international modes of accounting standard-setting and the importance that transnational corporate pressure plays in shaping and structuring standard-setting processes. This study involves standard-setting bodies in countries where the involvement of government plays a minor role in the standard-setting process, i.e., that accounting standard-setting is not conducted by an agency of government but rather by a group that is (more or less) independent of government.[13] This is an important point in that this circumstance allows for participation by MNCs, professional accounting associations, professional accounting firms, and individuals in the process. Government also has the opportunity to participate in the process, but the evidence on the development of standards for foreign currency shows that the state was less involved in developing the specific provisions of the standards as compared to the involvement by the MNCs which directly or indirectly affected the decisions made by the standard-setting bodies in these countries. In investigating the attempts by standard-setters in these countries to form an international consensus surrounding foreign currency accounting, this dissertation suggests that the activities of accounting standard-setters can be described as active intervention in a power struggle among specific MNCs and among

---

13

Robert Bloom and M. A. Naciri, "Accounting Standard Setting and Culture: A Comparative Analysis of the United States, Canada, England, West Germany, Australia, New Zealand, Sweden, Japan, and Switzerland", *International Journal of Accounting* 24 (1989): 70-97.

themselves over legitimation of authority in accounting regulation.

This study is also motivated by a concern over the evidence of current lobbying studies[14] in accounting literature. Accounting standard-setting has been argued to be a political process based on practical concerns, not on theoretical concepts.[15] This dissertation argues that it is indeed political, but not from a pluralist[16] point of view as most of these studies assume. The evidence in this dissertation builds on studies[17] that show little congruence between lobbyists' efforts and choices made by standard-setting bodies. This study shows the futility of positive work that attempts to predict lobbying efforts. Those studies have focused mainly on characteristics of lobbyists and their positions. If there is little correlation between comment letters and the outcomes of standard-setters' deliberations, then why focus on the characteristics of lobbyists? If it

---

14

For a review of these studies, see Carol Olson Houston, "Foreign Currency Translation Research: Review and Synthesis", *Journal of Accounting Literature* 8 (1989): 25-48, and also Chapter 4.

15

Lane A. Daley and Terry Tranter, "Limitations on the Value of the Conceptual Framework in Evaluating Extant Accounting Standards", *Accounting Horizons* (March 1990): 15-24.

16

"Pluralism" views entities within a society as having their own interests and having the potential for influencing decision-making regarding those interests. "Elitism" views society as composed of a ruling elite with the rest of society having limited influence in decision-making. "Radicalism" views society as composed of a dominant class in conflict with other classes (K. Robson and D. J. Cooper, "Power and Management Control", in W. F. Chua, E. A. Lowe, and A. G. Puxty (eds), *Critical Perspectives in Management Control* (London: Macmillan, 1989): 79-114).

17

M. J. Bryant, "Formal Lobbying Activity: The Case of FAS 8", Working paper (University of Toronto, 1988) and D. S. Solomons, *Making Accounting Policy: The Quest for Credibility in Financial Reporting* (Oxford, 1986).

appears that the interest of a few "powerful" organizations can influence the choices made by standard-setting bodies, what purpose then does predicting lobbyists' efforts serve? Also, what does this tell us about the nature and effectiveness of lobbying efforts? What does this tell us about the standard-setting process in which interested parties are permitted to voice their opinion, but in the end it may be only the voice of a few powerful MNCs that influence the development of accounting standards?

II. Foreign Currency Standards and Issues in International Accounting Harmonization

Foreign currency is the most international of all accounting standards because it directly involves the translation of assets and liabilities held or incurred in foreign countries. Because of the many jurisdictions that MNCs can potentially operate under, there are possibly as many approaches to dealing with the reporting of these assets and liabilities. The situation can become hopelessly confusing to users of financial statements in trying to compare the financial position of MNCs. Likewise, MNCs have a stake in the outcomes of deliberations on such standards. Their preferences for accounting methods depend upon the individual circumstances in which companies operate, the effects of different methods on company profits and the strategies by which companies strive to protect their foreign financial position. Some of these strategies limit foreign investment to specific countries only. Thus, the choices and strategies made by MNCs begin to affect the social and economic circumstances for nations as well as individual investors.

In the foreign currency story, a number of conditions at first glance appear feasible in explaining the choices made by standard-setting bodies in individual countries but closer examination reveals that deliberations included interactions among standard-setting bodies and between standard-setters and outside parties, mainly MNCs. This case of foreign currency standards provide an opportunity to examine the nature of such interactions and the possible effect on outcomes. To say, for example, that UK standard-setters were in favour of the current rate method does not indicate why the Accounting Standards Committee (ASC) endorsed it. What role did other groups play in that decision? What was the involvement of the MNCs in this process? What do the answers to these questions tell us about standard-setting in general and specifically about international harmonization?

Foreign currency accounting is appropriate to address the issues of harmonization in that it provides a unique situation in which all countries were affected differently but simultaneously by a worldwide phenomenon (the breakdown of the Bretton Woods agreement). Other accounting issues have been addressed in countries at different times. For example, inflation accounting was a concern in the UK in the late 1960's and throughout the 1970s but was not an issue in the US until the late 1970s. Standard-setting bodies might respond differently in developing standards at different times because bodies that addressed the issue earlier set a precedent which may influence another country's choices of methods. This is the case to some degree in the foreign currency story but early standards were in place for a very short time before other countries were pressured to act. Also, external conditions may change from one decade

to the next, creating more complications in isolating causal variables. The foreign currency issue minimizes any possible effects due to time differences because all these countries were concerned to resolve the issue at virtually the same time.[18] With fewer variables to be concerned with, the causal relations that represent impediments or aids to harmonization are more easily identified and the history of foreign currency accounting provides just such an opportunity.

The circumstances surrounding the controversies concerning international accounting harmonization are perhaps indicative of the changing nature of the relationship between regulatory institutions (such as accounting) and the state. With the globalization of business arose a change in the concept of the state and its ability to regulate business outside its borders. The concept of "state" has become more difficult to define in a global context.[19] As capital began to operate outside the jurisdiction of the

---

18

The Accounting Principles Board in the US considered developing a new standard on foreign currency in 1971 and the FASB placed it on its initial agenda in 1973. Foreign currency accounting had been on the agenda of the UK's Accounting Steering Committee (now the Accounting Standards Board (ASB)) since 1970 (P. Wallace and B. D. G. Ogle, "Foreign Currency Translation", *Selected Accounting Standards--Interpretation Problems Explained* (London: ICAEW, 1984): 201-254). The foreign currency project in Australia commenced in February, 1972 (from a history sheet from the files of the Australian Accounting Research Foundation (AARF)). Because of incomplete information about the Canadian Institute for Chartered Accountants (CICA), it is not clear when the topic was placed in the agenda, although the CICA published Parkinson's study on foreign currency in 1972. Also because of limited information about the IASC, it is not clear when they began working on foreign currency. However, there is correspondence between the then secretary of the IASC and the AARF in 1974 on foreign currency accounting.

19

David Held, "Introduction: Central Perspectives on the Modern State", in David Held, James Anderson, Bram Gieben, Stuart Hall, Laurence Harris, Paul Lewis, Noel Parker,

nation-state, the state began to function increasingly under the pressure of market forces. Regulation is characterized more in the sense of the ways in which "a global system of societies are brought together and 'managed' over space and time"[20] rather than by "rules which are laid down in law and enforced through specific processes of monitoring and supervision."[21]

The increase in the number of international governmental and non-governmental groups in the 1960s and 1970s[22] is also indicative of this shift towards regulation through managing global societies as opposed to regulation through enforcement of laws. Nation-states have become more and more integrated into international norms[23] and have lost some of their ability to control and monitor the activities of large corporations. Organizations such as the United Nations and the Organization for Economic Cooperation and Development (OECD) exemplify this way of governing on a global

---

and Ben Turok, eds., *States and Societies* (Oxford: Martin Robertson & Co., Ltd, 1983).

20

Glenn Morgan, "The Global Context of Financial Services: National Services and the International Political Economy", in G. Morgan and D. Knights, eds., *Deregulation and European Financial Services* (London: Macmillan, forthcoming).

21

A. Ogus, *Regulation: Legal Theory and Economic Forms* (Oxford: Oxford University Press, 1994), cited in Morgan, *ibid.*

22

The number of intergovernmental international organizations grew from 123 in 1951 to 365 in 1984 and the number of non-governmental international organizations grew from 2173 in 1972 to 4615 in 1984. (From Eric J. Hobsbawm, *Nations and Nationalism since 1789: Programme, Myth, Reality* (Cambridge: Cambridge University Press, 1990), cited in Frederick Buell, *National Culture and the New Global System* (Baltimore: Johns Hopkins University Press, 1994)).

23

Buell, *ibid.*

basis but without the power to enforce rules. Member countries in these organizations are loosely connected.

This condition is facilitated by the emergence of the neo-liberal concept of free trade which includes the free movement of capital and information across national borders. "Most countries accept the discipline of a free-trade system because they recognise that free trade is beneficial to everybody."[24] A harmonized system of accounting is part of an international financial system of regulation designed to facilitate free trade across national boundaries.[25] The need for such a system is exacerbated by the increasing demand for financial information by capital markets. The UN and the OECD both worked towards harmonizing accounting standards, but focused mainly on disclosure recommendations and not on developing standards for financial reporting per se.[26] The purpose of the IASC is to develop a set of standards, but like the UN and

---

24

"The Nation-State is Dead, Long Live the Nation-State", *The Economist* (December 23rd 1995-January 5th 1996): 15-18.

25

Morgan, *ibid.*

26

Richard D. Fitzgerald, "International Harmonization of Accounting and Reporting", *The International Journal of Accounting Education and Research* (Fall 1981): 21-32; Frederick D. S. Choi and Gerhard G. Mueller, *International Accounting, 2nd Edition* (Englewood Cliffs, N. J.: Prentice-Hall, 1992); Yukio Fujita "Recent Activities of the United Nations toward International Harmonization in Accounting and Reporting", in *Changing International Financial Markets and Their Impact on Accounting* (Champaign, Ill.: Centre for International Education and Research in Accounting, Dept. of Accountancy, 1992). Disclosure refers to reporting the methods and details of calculation, measurement, etc., concerning the elements of the financial statements. Standards are specific about what elements are to be reported, how valuation is to be determined (e.g., historical cost versus current market value), what methods of accounting are permitted, among other things. In simple terms, standards dictate how

OECD, it lacks the power to enforce its rules.

One might argue that differences in accounting rules have been shrinking in recent years[27] given the successful work of the IASC which has developed a tighter, more coherent set of international standards.[28] A meaningful set of widely accepted international accounting standards seems more plausible than ever before considering the progress of the IASC.[29] The process of developing these standards, however, has not been without its tensions. There are well known tensions in accounting standard-setting between standard-setting groups in the US and Germany, for example, whose approaches to financial reporting differ substantially.[30]

---

accounting should be conducted while disclosure asks for how it was conducted.

27 The Economist, "Bean counters, unite!" *The Economist* (June 10, 1995): 67-68.

28 The Economist, 1995, *ibid.*

29 In July, 1995, the IASC made an agreement with the International Organization of Securities Commissions (IOSCO), of which the US Securities and Exchange Commission (SEC) is a member, on a plan to develop a core set of accounting standards acceptable for financial reporting in cross-border securities offerings. (From Michael H. Sutton, "Financial Reporting in U. S. Capital Markets: International Dimensions", *Accounting Horizons* 11 (June 1997): 96-102.)

30 Standard-setters in the US, the UK, Australia, and Canada follow the Anglo-American approach to financial reporting which presents itself as adopting a purpose of aiding investor decision-making and requiring extensive disclosure (although the extent of disclosure does vary among these countries). The German view advocates the approach of "prudence" as opposed to the UK "true and fair view", and until the 4th Directive was adopted in 1985 in Germany, disclosure requirements were not spelled out in the German Commercial Code. German financial reporting has emphasized (and still does) the benefits for tax authorities and the protection of creditors who are more concerned about cash flow than they are about short-term profits. Consequently, German companies have an incentive to value assets at their lowest possible amount and liabilities at their highest

Much of this problem has been attributed to a lack of US acceptance of the IASs. Although most large national stock exchanges permit foreign firms to reports results according to the IASs, a few crucial ones, i.e., the US stock exchanges, don't. The US Securities and Exchange Commission (SEC) refuses to accept the IASs.[31] This position of the SEC is seen as a roadblock to the international harmonization of accounting standards. The chairman of the SEC has said that the SEC would be prepared to accept the international standards in a few years' time, provided certain differences in troublesome issues can be resolved (e.g., accounting for intangible assets and financial instruments).[32] However, the SEC supports the recent collaboration between IOSCO and the IASC to develop a core set of accounting standards and will consider allowing foreign companies to use IASs in securities offerings in the US.[33] At the same time, European firms view the US standards as excessively burdensome and consider that IASC's effort to tighten up it standards tilts its approach to financial reporting towards the US side.[34]

Other issues exist also. In the US, financial executives and the SEC are

---

amount to minimize their tax liability, even if this means departing from a true and fair view (From David Alexander and Simon Archer, *European Accounting Guide* (London: Harcourt Brace Jovanovich, 1991)).

31 The Economist, "Global accounting's roadblock" *The Economist* (April 27, 1996): 79-80.

32 *Ibid.*

33 Sutton, *ibid.*

34 The Economist, 1995, *ibid.*

displeased with the slow pace of the development of accounting standards by the Financial Accounting Standards Board (FASB). At the same time, the progress in developing international standards by the IASC might be seen as a threat to the purpose of the national standard-setting bodies in developing their own standards. Developing countries may also feel threatened by the overwhelming predominance of developed countries on IASC technical committees.[35] For example, the Arab Society of Chartered Accountants asked for help in developing accounting standards from international accounting firms, rather than the IASC.[36]

The US influence is also seen through the workings of the G4. The G4--standard-setting groups in the UK, the US, Australia, and Canada--is working to coordinate the development of accounting standards in these countries and with the IASC.[37] It could appear that, although this collaborative effort assists the IASC, it provides opportunity for further strengthening the Anglo-American or, perhaps, US, influence in international accounting standard-setting. As long as international standard-setting bodies align their

---

35

Between 1973 and 1989 46 technical committees established by the IASC were composed exclusively of members from developed countries. From Haim Falk, "International Accounting: A Quest for Research", *Contemporary Accounting Research* 11 (Fall 1994) : 595-615.

36

Ibid.

37

David Cairns, "Time for turf warriors to reach a peace accord" *Financial Times* (May 16, 1996). Some of the current issues being worked on among these countries include reporting financial performance, hedging and derivatives, segment disclosure, business combinations and intangible assets, and present-value measurements (From Financial Accounting Standards Board, *Financial Accounting Series: Status Report No. 284* (January 14, 1997).

approaches to financial reporting with the US approach, harmonization (in the sense of acceptance by some key players) is feasible. Without the SEC's blessing, roadblocks continue to exist, according to the popular press. One could argue that as long as the G4 continues to exert its influence on the IASC, acceptance by the US of the IASs is more likely. Evidence suggests that the IASs are becoming more and more like the US standards. Recently, for example, both the FASB and the IASC approved drafts for public exposure on earnings per share that are almost identical.[38]

The recent circumstances in accounting standard-setting involving tensions between differing approaches to financial reporting (e.g., German view vs the US view)[39], seeming blockages by the SEC in effecting a global set of accounting standards, and various threats to the effectiveness of national standard-setting bodies suggest a strong influence of standard-setting bodies in a single country (the US) or a group of countries (the G4) on the development of international accounting standards. These circumstances can lead to questions such as, "Who really influences, aids, or hinders the processes involved in international accounting standard-setting? Do the SEC rules really hinder harmonization?". The evidence in this study suggests that hindrances to harmonization cannot be reduced to differences in approaches to accounting between countries or to the hegemony of a single entity. Rather they extend to different

---

38

IASC Insight (March 1996).

39

Other tensions include the differences in flexibility between UK and US accounting standards.

approaches taken to resolve specific accounting problems due to different jurisdictions in which companies may be operating, a company's corporate structure or other internal situations (such as performance measures for subsidiaries, for example) and the preferences for these approaches expressed by MNCs. To what extent these preferences by MNCs influence the national differences among accounting standard-setters is the subject of this dissertation.

In order to more fully understand the complex nature of developing a foreign currency standard and its implications for MNCs, the next section of this chapter recounts the events that led to a change in accounting for foreign currency. The section emphasizes the significance of the downfall of the Bretton Woods agreement and the expansion of foreign business by MNCs in creating an impetus for the debates on foreign currency accounting that coincided with these events.

III. The Political and Economic Context of Foreign Currency Accounting

The developments in accounting for foreign currency arose from a complex series of macroeconomic and political events and circumstances of the late 1960's and early 1970's. This section discusses how these events and circumstances had implications for accounting and accounting standard-setting. This narrative focuses not just on the perspectives of different accounting approaches found in different countries, but on the variation in perspectives within countries. Harmonization is not just a country problem. The interests of different users and preparers can vary as much within a country as

between countries.

The Foreign Exchange Rate System: 1944 onwards

World War I and the world depression of the 1930's disrupted the world monetary order and led to a conference in July 1944 at Bretton Woods, New Hampshire, in which 44 nations agreed to set up the International Monetary Fund (IMF).[40] The role of the IMF was to provide its members with a code of conduct concerning international payment restrictions and exchange rates and to provide liquidity for its members in official transactions in the foreign exchange market.[41] The US dollar was chosen as the numeraire of the system, which meant that other member countries defined their currency values in terms of dollar par values.[42]

This arrangement created problems for the US in adjusting "fundamental" imbalances of the dollar which became apparent with the balance of payments deficit in the late 1950s.[43] In part, the deficit was the result of the Marshall Plan which pumped

---

40

Excellent sources on the developments of the Bretton Woods agreement and the exchange rate system in general include Stanley W. Black, *Floating Exchange Rates and National Economic Policy* (London: Yale University Press, 1977); Fred L. Block, *The Origins of International Economic Order: A Study of United States International Monetary Policy from World War II to the Present* (Berkeley: University of California Press, 1977); Armand Van Dormael, *Bretton Woods: Birth of a Monetary System* (New York: Holmes & Meier Publishers, Inc., 1978); and Brian Tew, *The Evolution of the International Monetary System: 1945-85*, 3rd ed. (London: Hutchinson, 1985).

41

Tew, *ibid.*

42

Black, *ibid.*

43

Ibid.

many US dollars into Europe for restoration after World War II. European central banks accumulated dollars in their reserves which led to an increase in the demand for gold. Consequently the Eurodollar market developed which allowed the lending or investing of dollar deposits in Europe. These conditions set the stage for volatile short-term capital movements (motivated by interest rate differentials and speculation concerning gains and losses from changes in exchange rates) and the growth of the internationalization of financial markets which created the means for huge flows of funds across national borders.[44]

The disequilibrium in world payments continued throughout the 1960's. Speculative borrowing increased so foreign banks were buying dollars on a large scale to prevent appreciation of their own currencies against the dollar.[45] Besides increased global financial activity, a lack of consideration given to financing the war in Vietnam and US political events associated with it contributed to the worsening of the US trade position and, because of the dominant place held by the US in the world economy, contributed to the instability in international financial markets.[46] Ultimately, the worsening conditions of the US balance of payments prompted the US to temporarily suspend the convertibility of the dollar into gold in 1971. Other countries responded by

---

44

Tew, *ibid.*

45

Ibid.

46

Anthony Woodiwiss, *Postmodernity USA: The Crisis of Social Modernism in Postwar America* (London: Sage Publications, 1993).

"unpegging" their currencies from the dollar. Later that year ten nations[47] met in Washington, D. C., and drafted the Smithsonian Agreement in which they agreed to re-peg their currencies on the dollar at new central rates (except for the Canadian dollar which remained floating).[48]

The Smithsonian Agreement was short-lived, however. In 1972, the British balance of payments began to deteriorate and the surplus at the beginning of the year turned into a deficit by the end of the year. The Chancellor of the Exchequer announced in June that the British pound would be allowed to float. The sixty-five or so nations that pegged their currencies on sterling discontinued the sterling peg and replaced their sterling reserves rapidly with dollar reserves,[49] thus increasing the demand for dollars even more.

The fact that the dollar could be devalued via techniques like the Smithsonian Agreement suggested that it could be devalued again. This realization led to a lack of confidence in the Smithsonian currency values and to speculation in the price of gold and runs on the dollar in 1973 (also exacerbated by the oil crisis of 1973-74). After two crises, in February and March, 14 countries (the G-10, Switzerland, Denmark, Luxembourg, and Eire) met and agreed to a floating system, some countries jointly and

---

47 The US, Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Sweden, and the UK (known as the G-10) (Tew, *ibid*).

48 *Ibid.*

49 *Ibid.*

others individually.[50] This marked the end of the fixed exchange rate system.

The Globalization of Business

The Marshall Plan was only partially responsible for the outflow of capital from the US. Contributing to the outflow were massive amounts of foreign investments abroad by US companies. An example of the extent of this foreign investment is the case of General Electric which increased the number of foreign plants from 21 in 1949 to 82 in 1969.[51] Between 1950 and 1964, the proportion of US corporate profits based on foreign investment increased from 10% to 22%.[52] A survey of 298 of the largest US corporations showed that by 1970 they obtained 70% of their profits abroad.[53]

Capital flows across borders were also aided by foreign investment from companies in other countries. The German textile and garment industry more than doubled its foreign employment from 1966 to 1975. By the mid-1970's, the number of workers employed by West German companies in foreign countries amounted to 20% of total domestic employment. In Sweden, foreign investments increased 80% between 1960 and 1965. The total number of employees of Swedish-owned foreign firms grew four times faster than the growth rate of domestic employment during the same time

---

50 *Ibid.*

51 Scott Lash and John Ury, *The End of Organized Capitalism* (Madison, WI: University of Wisconsin Press, 1987).

52 Woodiwiss, *ibid.*

53 Lionel Cliffe, "Modern World Capitalism and its Contemporary Crisis", in David Coates and Gordon Johnston, eds., *Socialist Strategies* (Oxford: Martin Robertson, 1983).

period.[54]

These global developments are the result of what has been labelled the "disorganization of capitalism" by some authors[55] or the "crisis of Fordism" by others.[56] Characteristic of capitalist disorganization is the increase in global activity by MNCs[57], attributed in part to the fall in the rate of profit in western manufacturing activity. Fordism refers to a regime of intense accumulation experienced by capitalist societies beginning in the 1920s in the US and intensifying after World War II. It was made possible by increased surplus-value due to the mechanization of the labour process through implementation of assembly-line production and Keynesian economic welfare policies. The crisis of Fordism refers to the inability of the system to maintain levels of surplus value necessary to continue the rate of increase in corporate profits characteristic of early Fordist production,[58] prompting corporations to extend operations beyond domestic borders in search of cheaper modes of production. The crisis was further aided

---

54 Lash and Ury, *ibid.*

55 *Ibid.*

56 Alain Lipietz, *Towards a New Economic Order: Postfordism, Ecology and Democracy* (New York: Oxford University Press, 1992).

57 It is termed "disorganized" in the sense that nation-states lost some of the control of corporate activity as MNCs operated in jurisdictions outside of the domestic country and that international financial markets were not regulated by any government or international agency (Lash and Ury, *ibid*).

58 Michel Aglietta, *A Theory of Capitalist Regulation* (London: New Left Books, 1979) and Lipietz, *ibid.*

by the increased cost of the Keynesian welfare state which had been designed to maintain a minimum level of consumption.[59]

As some national corporations became multinational, they moved beyond the confines and controls of the nation-state.[60] The liberal state had delegated the task of governing firms and families through a body of experts[61] (including accounting professionals and standard-setters). The multinational firm has become increasingly more influential on this body of experts and on the state. The evidence suggests that this was indeed the case for accounting standard-setting for foreign currency for the countries in this study.

Globalization of business was aided by the development of computerized systems of information which allowed for the monitoring of operations in different parts of the world and by the growth in international money markets (i.e., the Eurodollar market) which enabled MNCs to engage in financial speculation in the exchange rate and interest rate markets. The massive overseas investment by US companies was accompanied by increased borrowings by these companies from foreign banks. Private lending by Eurocurrency banks grew at a phenomenal rate, from $44 billion in 1969 to

---

59 Lipietz, *ibid.*

60 Cliffe, *ibid.*

61 Michel Foucault, "Questions of Method", in Graham Burchell, Colin Gordon, and Peter Miller, eds., *The Foucault Effect: Studies in Governmentality* (Chicago: University of Chicago Press, 1991); Peter Miller and Nikolas Rose, "Governing Economic Life", *Economy and Society* 19 (February 1990): 1-69.

$810 billion by 1980. As mentioned previously, the increase in the movement of capital subjected national economies to balance of payments crises, particularly for the US and Britain,[62] but also created special accounting problems for corporations holding foreign assets and liabilities.

Implications for Accounting and Accounting Standard-Setting

Historically foreign currency was a very important and controversial topic facing MNCs, accountants, regulators, governments, and accounting standard-setting bodies. It arose as a result of events in the political economy (the breakup of the Bretton Woods agreement and the switch to a floating exchange rate system) that affected virtually all countries of the industrialized world. The issues involved the implications of the switch from a fixed exchange rate system to a floating rate system, the development of accounting standards to cope with the new system, the harmonization of these standards, and the differential effects that the same accounting method could have on different companies in different industries and operating environments.

The switch from a fixed rate system to a flexible rate system is thought to have created economic and political instability in international trade, resulting in financial markets and instruments to provide the liquidity designed to protect banks and companies from the financial risk that floating rates created. Before the advent of flexible rates, national and international financial systems operated in a relatively stable environment guaranteed by an international trading system with fixed exchange rates

---

62
Cliffe, *ibid.*

backed by a single dominant currency. The instability that resulted from the flexible rate system forced national financial systems to change their own financial institutions. The stability that was no longer achieved by a fixed rate system was potentially brought about through markets with the liquidity which enabled traders (primarily banks and companies) to purchase foreign exchange as they saw fit. These traders protected themselves from falls in the exchange rate by engaging in hedging strategies. This system could not operate unless traders could respond rapidly to changes in the value of currencies, resulting in 24-hour trading and a speculative nature to the trading of foreign exchange. The markets that developed to accommodate this type of activity changed the way that the international political economy operated. Instead of a standard of monetary value embodied in gold and fixed exchange rates, value is determined by the market. These markets also allow national financial institutions to trade internationally, thus increasing cross-borders flows of capital and competition among these markets and global financial institutions.[63]

The nature of this system is rather precarious in that there is no governing body to enforce rules and maintain order. The system depends on market processes. The complex nature of competition in these markets makes the creation of international regulatory institutions difficult to develop, enforce, and maintain.[64] This characteristic applies to all financial institutions and markets, including banks, stock markets, foreign

---

63 Morgan, *ibid.*

64 *Ibid.*

exchange markets, etc. The competitive nature of this system is one that does not necessarily support the development of standards or rules for monetary order, including accounting standards. The competition for information is strong but can also inhibit the free flow of capital. The alleged problem in the US of attracting foreign issuers to US stock markets is an example of how the difference in accounting standards might restrict opportunities for raising capital by non-US companies. The acceptance of IASs by non-US members of IOSCO may give them a competitive edge over the stock markets in the US which are prohibited by the SEC from accepting financial statements prepared according to IASs.

Flexible exchange rates create problems for multinational companies in consolidating financial statements between parent companies and foreign subsidiaries. Foreign subsidiaries are independent legal entities but in many countries, the parent and subsidiary companies are treated as single entities for accounting purposes. Thus, a single set of financial statements must be prepared that consolidates the financial statements of the parent and subsidiary companies. The problem arises when financial statements of the foreign subsidiary are prepared in the local currency and its assets and liabilities must be translated to the parent company currency. Financial statements cannot be prepared using multiple currencies and are typically prepared using the currency of the parent company. Translation is the process of restating accounts prepared in foreign currencies to single currency equivalents. Translation is necessary to record any foreign currency transaction, as in import and export activities, and for reporting the activities of branch and subsidiary operations.

Parent companies have reasons for maintaining accounts in the local, or foreign currency. Many companies hire local managers who are used to operating in local currencies. Comparison of financial data with other local companies is facilitated when accounts are prepared in the local currencies. The expansion of multinational corporate activity increases the need to convey information from one company to a number of readers in various domiciles as companies seek to raise capital in foreign markets. To make the information relevant to foreign readers, companies will sometimes translate their financial statements to the currency of the reader's country.

Problems associated with translation stem from flexible exchange rates. With the daily fluctuations in exchange rates, it becomes difficult to know what exchange rate to use in the translation.[65] For example, which exchange rate should be used to value an asset, the rate on the day that the asset was purchased or produced or on the day that the financial statements were prepared? When exchange rates were fixed, it mattered little what rate was used because the rate did not vary significantly, unless there was a decreed devaluation. But with the advent of flexible rates, exchange rates can vary daily according to the movements of the currency markets.

Many different translation methods have been used in practice by MNCs, making it difficult for investors and other interested parties to compare financial reports among

---

65 For an example of the effects of fluctuating exchange rates on company operating and financing decisions, see Leonard M. Savoie, "Financial and Accounting Aspects in International Business", *The International Journal of Accounting Education and Research* 9 (1973):13-22.

companies.[66] As global activity increased in the late 1960's and exchange rates became flexible in the early 1970's, the problem associated with accounting for foreign currency translation for MNCs centered on avoiding accounting losses due to fluctuations in exchange rates. The increased borrowings along with the increase in operations overseas created special accounting problems for MNCs as more and more assets and liabilities were denominated in foreign currencies whose exchange rates were no longer fixed as of 1973. The combination of dollar devaluations in the early 1970s and upward revaluations of other currencies at the same time, along with certain new borrowing restrictions in some countries, led one US corporate manager to believe that his company could no longer protect the company from foreign exchange variations when either the US dollar or foreign currencies decline or increase in relation to each other.[67]

The increased risk in keeping a balanced position in assets and liabilities and in avoiding losses from changes in foreign currency rates led to calls for establishing new guidelines for accounting for foreign currency translation, not only on a national basis but ones which would be universally accepted. A concerted effort towards international accounting harmonization was just beginning in 1973 (the year that the IASC was established). The predicament in accounting for foreign currency translation coincided

---

66

One might argue that the choice of methods may allow managers to signal private information and is therefore more informative. This would suggest that managers of MNCs might be opposed to a mandatory set of accounting rules which would eliminate that option.

67

Ibid.

with a growing awareness of the diversity of accounting practices worldwide. Thus, the call for developing and harmonizing foreign currency accounting from a financial statement user's perspective could have emerged from a general desire to reduce the diversity in accounting practices. The advent of the flexible exchange rate system made the foreign currency issue more pronounced.

Controversies centered on various methods' effects on subsequent years' financial statements and the volatility of earnings, which could result in lower share prices.[68] Research results on the stock price effects of adopting different foreign currency pronouncements vary according to statistical methods used[69] so it is not clear whether the market actually responds to the adoption of different accounting treatments for foreign currency or whether the results are due to flaws in research methods. However, concerns over the effects on financial statements led managers to engage in strategies to protect net asset or net liability positions of foreign operations. These strategies include hedging, cash flow control measures, accelerated dividend remittances, more local borrowing, and tighter monitoring and control of economic exposure.[70] The creation of a market for innovative international financial instruments, such as currency

---

68

Robert Van Riper, *Setting Standards for Financial Reporting: FASB and the Struggle for Control of a Critical Process* (Westport, CT: Quorum Books, 1994); William F. Messier, Jr., "SFAS No. 8: Some Implications for MNCs", *The International Journal of Accounting Education and Research* 14 (Spring 1979): 101-119.

69

Houston, *ibid.*

70

Irving L. Fantl, "Problems with Currency Translation--A Report on FASB No. 8", *Financial Executive* (December 1979): 33-36.

swaps, foreign currency options, and cross-currency swaps enabled the management of foreign exchange risk as corporate managers sought to transfer these risks to parties willing to assume them.[71] More local borrowing means that more debt is denominated in the domestic country's currency. That has macroeconomic implications for the US in particular, because it results in more liabilities held in US dollars, which was one of the conditions that led to the run on the dollar in the early 1970s and the suspension of the gold standard. It is believed that a balance between US dollar and local currency debt sourcing is preferred.[72] Because of these issues, there was concern also that to minimize the risk in maintaining balanced positions, companies might engage in shifting foreign investment to only those countries in which currencies are relatively stable which would reduce investment in less developed countries that were short of capital.[73] In the UK standards for foreign currency, the provision which allowed differences on borrowings to be offset against differences in assets in the same currency was likely to result in the deterring of borrowings in currencies not matched by offsetting assets in the same currency.[74] The UK parent company would borrow only in sterling or in the subsidiaries'

71

Frederick D. S. Choi and J. Matthew Singleton, "Accounting for Derivative Products", in Frederick D. S. Choi, ed., *Handbook of International Accounting* (New York: John Wiley & Sons, Inc., 1991).

72

Laurence J. Mauer, "MNCs Gain New Freedom Under FAS 52 Flexibility", *Management Accounting* (December 1983): 30-33.

73

William F. Messier, Jr., " SFAS No.8: Some Implications for MNCs", *The International Journal of Accounting Education and Research* 14 (Spring 1979): 101-119.

74

This provision was changed in the final draft of the UK standard to permit offsetting

local currency. Those companies with currency borrowings not matched by assets in the same currency would likely consider liability assumptions by a third party or long-term forward contracts to eliminate the effect of currency fluctuations on the profit and loss account.[75] Thus, there were significant social and economic consequences of the accounting methods used.

From a preparer's perspective, the issue concerns finding a method of accounting that would safeguard the company against the economic and accounting problems that the flexible exchange rates created. The problem for individual companies was not just over dealing with the fluctuating nature of exchange rates. The debate concerned what methods of accounting were most acceptable among preparers of financial statements, which varied depending on the companies' specific situation, and concerned the effects on the companies' profit margins. The same accounting procedure can have vastly different effects on company profit depending on the amount of assets and liabilities held in foreign currency.[76] Company-specific issues are very significant in this study because

---

against foreign assets not denominated in the same currency. However, the US standards require the offset to be in the same currency.

75

Michael Portington, "Foreign Currency Translation: The New Accounting Approach", *Accountancy* (February 1981): 105-107.

76

For example, second quarter financial statements in 1981 for two major US corporations showed that one incurred a $174 million cut in profits while the other reported a 77 per cent gain in profit due to accounting rules for foreign currency ("Accounting Rule Distorts Multi-nationals' Reporting", *Globe and Mail* (August 6, 1981)). Also, the effect of adopting FAS 52 by 24 US companies in 1981 resulted in changes in foreign income after taxes ranging from 0% to 66.7% for 23 companies (for one company it was a change of -11.4%) (From Mauer, *ibid.*)

the issue of harmonization of accounting standards is not just among standard-setting bodies in different countries, but also among MNCs operating in many different accounting jurisdictions, economies, and social structures along with varying company policies, practices, and strategies that can vary even among companies within the same industry, let alone the same country. There are an infinite number of company-specific situations that may result in preferences for one method of accounting over another which may explain the involvement by the MNCs in the process of developing accounting standards for purposes of preserving their preferred method. Understanding the nature of these different viewpoints of preparers helps to understand the difficulties associated with harmonization. It helps us to understand how power begins to play a role in the development of an "acceptable" standard. Acceptable to who? Presumably, acceptability concerns those who have the power to influence, persuade, align, and enroll the bodies with the responsibility for developing these standards so that their preferences for accounting methods are protected.

IV. Conclusion

The combination of increased global activity and a floating exchange rate system created special accounting problems for preparers and users of financial statements in the early 1970s. Efforts towards harmonization of accounting practice were just underway at that time. The problems of translating financial statements became much more apparent as corporate management attempted to protect companies from foreign exchange risk due

to fluctuating currency exchange rates. Accounting standard-setters faced a challenge to develop a set of guidelines to provide comparable information for users of financial statements.

The accounting standard-setting process is similar in the countries of the US, the UK, Australia, and Canada. Along with the similar orientation towards financial reporting for investor decision-making, the environment in these countries made it possible for standard-setters to attempt harmonization of foreign currency standards. Differences between the Anglo-American and German approaches to standard-setting are apparent enough but differences of opinion also exist among standard-setting bodies in the US, the UK, Australia, and Canada. The history of the development of foreign currency accounting bears this out. This study explains how the standard-setting bodies in the US, Canada, the UK, and Australia responded in different ways to the monetary crisis of 1970s that affected accounting standard-setting bodies in all countries and how they eventually developed a greater degree of consensus.

This dissertation employs a comparative historical analysis to demonstrate that certain factors that existed among these standard-setting bodies serve as part of the structural conditions in which standard-setting for foreign currency took place, not as explanations for the choices made by standard-setting bodies in developing these standards. The comparative methodology employed in this work examines explanations beyond cultural hindrances to harmonization. Instead, it examines such factors as current practice, application of accounting principles, currency movements, lobbying efforts, and tax laws which can be argued to have justified the decisions made by standard-setting

bodies and are based on statements made in the documentation and published articles on foreign currency accounting.[77] However, a closer examination shows that they only partially account for the choices made.

The dissertation also reports on a more in-depth study of the history of the development of the standards in these countries to illustrate the role, and the effect, of networks of alliance in the social relations between standard-setting bodies and MNCs in the standard-setting process. The story of the development of standards for foreign currency accounting undermines a perspective that the US dominated international accounting standard-setting. While other countries have looked to the FASB for guidance in this area, few countries, even among the English-speaking nations, were willing to blindly follow the FASB example in the foreign currency case. Thus, while it may appear that the US (ie., the FASB or the SEC) has the power to impede the process of international harmonization, standard-setting bodies in other countries have the power to resist the influence of a major player. A study of the development of standards for foreign currency accounting among the US, the UK, Australia, Canada, and the IASC that includes an analysis of power provides an opportunity to demonstrate that the differences that do exist among accounting standards are not completely explained by the hegemony of a single entity or a set of specific conditions. Rather they are explained by interactions among national standard-setting bodies and between standard-setting bodies and outside parties in which conflict affects outcomes which may either impede or aid

---

[77] Citations are too numerous to mention here but are specified in Chapters 2 and 3.

the efforts towards harmonization.

The remainder of the dissertation is organized as follows: Chapter 2 begins the comparative historical analysis of certain conditions or factors existing through the 1970s and the 1980s which may serve as explanations of the choices made by standard-setting bodies in developing foreign currency standards. This analysis begins with the effects of currency fluctuations on these choices. Chapter 3 continues the comparative analysis of additional factors including current practice, accounting principles, tax laws, and the efforts of lobbyists. Chapter 4 reviews current theories of power and offers an analysis of social relations between standard-setting bodies and MNCs based on theories of power. Chapter 5 provides a brief summary of the findings of the study, further implications of the study, limitations, and additional questions raised for further research.

CHAPTER 2. ACCOUNTING FOR FOREIGN CURRENCY TRANSLATION

In the history of the development of foreign currency accounting, standards evolved from the endorsement of diverse translation methods and treatments for gains and losses among the US, the UK, Canada, and Australia, to some degree of harmonization of methods and treatments among these same countries. An argument explaining the diversity might point to certain conditions that differed for each country. These conditions or factors could be offered as explanations for the choices made by the standard-setting body for a given country. A comparative history would suggest that variations in actors' choices and outcomes were due to these differences. What effects these differences had on harmonization and how they were resolved are also relevant for understanding the consensus that eventually occurred.

Several factors could be argued as plausible explanations for the choices made by standard-setting bodies in developing standards for foreign currency accounting. This dissertation examines five of these possible factors. The purpose of this analysis is not to eliminate these explanations but to show that issues regarding the choices remain unresolved in light of these factors. The factors examined in this study are referred to in the debates on foreign currency accounting. The examination of these factors reveals that they only partially explain the outcomes of standards for foreign currency accounting.

The purpose of this chapter is to begin analysing the choices made by standard-setting bodies concerning method of translation and treatment of gains and losses in

developing standards for foreign currency accounting. The comparative analysis examines each case (standard-setting bodies in the US, the UK, Canada, Australia, and the IASC) longitudinally through the development of the standards. The examination of the individual cases will allow for an assessment of the effects on international harmonization. The Method of Difference, explained in the next section, is used in this analysis. The choices for method of translation and treatment of foreign currency gains and losses made by standard-setting bodies are the outcomes. The analysis discusses the similarities among the cases and focuses on the factors which set the cases apart. Five factors, current practice, accounting principles, currency fluctuations, lobbying efforts, and tax laws, are identified as potential variables that offer a causal explanation of the outcomes. Though this list of differences is not complete, it includes the most frequently suggested factors which have had a major impact on the choices made by the standard-setting bodies.

This chapter examines one of these factors, i.e., currency fluctuations. The choice of examining currency movements as a basis for the choices made by standard-setting bodies originates with the cynicism that had been directed toward the FASB when the Board decided to reconsider FAS 8.

> Cynics will suggest that this change of heart reflects the recent weakness of the dollar--and it was forced upon the FASB because American accounts were showing heavy losses, and that when the dollar was strong, and healthy profits on exchange were being shown by US companies, there was no incentive to change to the 'closing rate' method.[1]

---

[1] "Getting to grips with accounting Standards", *Accountancy* 90 (September 1979): 22.

This factor was also noted in ED 27 in the UK:

When the domestic currency of the holding company is one of the hardest currencies in the world, the conventional 'temporal' method (such as that required by Financial Accounting Standard No. 8 in the USA) produces an acceptable result. But when the consolidated financial statements are drawn up in a currency which is not the hardest, the temporal method can produce results which do not make commercial and economic sense and alternative solutions must be considered.[2]

(It is not clear from this comment what is really meant by "economic sense").

Opposition to FAS 8 also occurred when the US dollar strengthened:

the wide swings in profits caused by the strengthening U.S. dollar this spring have reinforced opposition to what many regard as lopsided and impractical procedures....The dollar's rapid rise against many foreign currencies this spring, as filtered through the accounting rule [FAS 8], has caused unusually large distortions...As a result, many believe that the health of the multi-nationals' core businesses frequently is hard to determine.[3]

The question is whether or not the decision to adopt the current rate method by FASB was motivated by the weakening of the dollar.

The following excerpt suggests that currency fluctuations in one country and the relationships between currencies in different countries does not necessarily result in the same accounting rule to be applicable to each situation:

solutions to translation problems as recommended by American authorities...cannot simply be accepted as being necessarily suitable to the Canadian situation [because of the relationship between the Canadian dollar and the US dollar]. A history of rate changes in the pound sterling since World War II also rules out British solutions as being automatically suitable to the Canadian

---

2

Accounting Standards Committee, "ED 27: Accounting for Foreign Currency Translations, *Accountancy* (December 1980): 119-126.

3

New York Times Service, *ibid.*, 1981.

situation.[4]

This investigation attempts to bring forth evidence concerning any consistency between the relative strengths of currencies with decisions made by standard-setting bodies.

Part I describes the Method of Difference used in the comparative analysis. Part II compares the responses of accounting standard-setters to the circumstances of the 1970s to acquaint the reader with the nature of the differences in the standards for foreign currency in the countries in this study. Part III presents the development of standards for foreign currency accounting as a response to currency crises and begins the comparative analysis by examining the possible association between currency fluctuations and the choices made by standard-setting bodies. Part IV provides concluding remarks.

I. Method

Comparative Analysis

This study employs two types of analysis. The first type is a method of comparative historical analysis. Variations and dissimilarities are explained in a comparative analysis which provides a check against over-generalization.[5] The method

---

[4] R. MacDonald Parkinson, *Translation of Foreign Currencies* (Toronto: CICA, 1972).

[5] T. Skocpol, *States and Social Revolutions: A Comparative Analysis of France, Russia, and China* (Cambridge: Cambridge University Press, 1980): pp.36-40.

employed in this study is similar to Weir and Skocpol's[6] analysis of the variation in nation-states' responses to the Great Depression. Skocpol discusses how comparative historical analysis works.

> Basically one tries to establish valid associations of potential causes with the given phenomenon one is trying to explain. There are two main ways to proceed. First, one can try to establish that several cases having in common the phenomenon one is trying to explain also have in common a set of causal factors, although they vary in other ways that might have seemed causally relevant. This approach is what Mill called the 'Method of Agreement.' Second, one can contrast the cases in which the phenomenon to be explained and the hypothesized causes are present to other cases in which the phenomenon and the causes are both absent, but which are otherwise as similar as possible to the positive cases. This procedure Mill labelled the 'Method of Difference.' Taken alone, it is a more powerful method than the Method of Agreement alone for establishing valid causal associations (provided that one can find suitable negative cases for the required contrasts). In practice though, it is often possible, and certainly desirable, to combine these two comparative logics. This is done by using at once several positive cases along with suitable negative cases as contrasts.[7]

The Method of Agreement attempts to explain why all cases arrived at outcome Y, given the overall differences among the cases. The investigation determines that there are one or more explanatory variables, X, that are present among the cases and that can logically explain Y. In the Method of Difference, outcomes are different among the cases. The intent is to compare "instances in which [a] phenomenon does occur, with instances in

---

6 M. Weir and T. Skocpol, "State Structures and the Possibilities for 'Keynesian' Responses to the Great Depression in Sweden, Britain, and the United States", in P. B. Evans, D. Rueschemeyer, and T. Skocpol (eds), *Bringing the State Back In* (Cambridge: Cambridge University Press, 1985): 107-163.

7 *Ibid.*

other respects similar in which it does not". [8] The cases are similar in many respects, variables A, B, C,...N, except for one or more variables, X and not X, that differ for the cases. These differences are shown to logically explain the differences in outcomes. (See Appendix I for a representation of this discussion.)

One of the problems with comparative analysis is overcoming the "many variables, few cases" problem. Statistical methods of analysis are not feasible when many variables can explain the phenomenon under question and few cases are available for investigation. The Method of Difference overcomes that problem by focusing on comparable cases, those that are similar in a large number of important characteristics to be treated as constants, but dissimilar with respect to certain phenomena which are to be explained.

The method in this study most closely resembles the Method of Difference. The aim is to identify cases that are similar on many grounds in order to explain the differences in accounting outcomes.[9] The accounting outcomes (the dependent variables) in this analysis are the choices made by standard-setting bodies concerning 1) translation method and 2) methods for handling translation gains and losses for foreign currency accounting standards. These are two outcomes or two phenomenon to explain,

---

[8] From John Stuart Mill's *A System of Logic*, 8th ed. (London: Longmans, Green, Reader, & Dyer, 1872) Book III, Ch.8, quoted in Arend Lijphart, "Comparative Politics and the Comparative Method", *American Political Science Review* 65 (1971): 682-693.

[9] Helen Gernon and R. S. Olusegun Wallace, "International Accounting Research: A Review of its Ecology, Contending Theories and Methodologies", *Journal of Accounting Literature* 14 (1995): 54-106.

so there are two levels of comparative analysis, one concerning translation method and the other concerning methods for handling gains and losses.[10] As the analysis shows, these choices were the most controversial issues and varied among the countries under study. These choices also varied over time as these standard-setting bodies moved towards harmonization.

The Method of Difference requires that a certain number of explanatory variables or causal factors be similar among the cases so as to establish the claim that any characteristic that varies among the cases is indeed the one that explains the different outcomes. The purpose or approach to financial reporting, the role of the state, and the standard-setting process are the overall similarities of these countries relative to continental European and Asian countries. The US, the UK, Australia, and Canada have in common the obvious characteristic of language, but more importantly a common approach to financial reporting. The US, the UK, Australia, and Canada base their approach on providing information for investor decision-making. Consequently, preparers (companies) are interested in reporting techniques that may enhance share price. These countries also employ a similar process in the development of accounting standards in which constituents have the opportunity to respond to discussion memoranda and/or exposure drafts of a proposed standard. The standard-setting body then examines the responses and may or may not take them into account in the release of

---

[10] These two issues, however, are not treated as independent of each other. The analysis demonstrates that they are somewhat interrelated.

the final standard. Also, an external task force is often used for each project, [11] thus providing an opportunity for outside parties to participate in the process. These procedures are more common in those countries where the standard-setting body is a relatively independent entity. In continental Europe and Japan, the main group that develops accounting standards is an arm of the government and the emphasis is on creditor protection (mainly Germany) and is based on court case law and tax law. Consequently, instead of reporting to enhance share price, the approach favours tax minimization.[12]

A weakness of the Method of Difference is that these similarities may not be sufficient to suggest that outcomes should not vary among the cases. Another weakness of this method is assuming that in the midst of all the similarities there is only one differing characteristic that logically explains the outcomes. That is the case with this study, for indeed, outcomes for foreign currency standards may be attributed to several factors, not just one. Possible factors include current practice, accounting principles, currency movements, lobbying efforts, and tax laws. In addition, other factors may exist that may provide "common sense" explanations. In this regard, the method in this study does not rigidly follow the Method of Difference because outcomes may be attributed to

---

[11] Bloom and Naciri, *ibid.*

[12] Dr. Wolf Kroneberger and Peter H. Combrink, *Accounting and Auditing in Germany* (Frankfurt, Germany: Coopers & Lybrand, 1991); Coopers & Lybrand, *International Accounting Summaries: A Guide for Interpretation and Comparison* (New York: John Wiley & Sons, 1991).

one or more "differing" factors. Hence, the Method of Difference is applied to the five factors mentioned above for each of the two outcomes to be explained during the time period to include the development of different standards among these countries to harmonization.

The analysis deviates from the Method of Difference in one other regard, and this is a crucial aspect of this analysis. That is, instead of explanatory variables for the methods and treatments chosen, these factors serve instead to depict the conditions in which standard-setting for foreign currency took place. The differences in the choices made by standard-setting bodies are not fully explained. However, the Method of Difference does provide a logical way in which to proceed. For if similarities exist among the cases, and if differing variables do not explain the outcomes, then one has to assume that something is being overlooked in the analysis.

The comparative analysis proceeds as follows. First, the questions under study are raised: why, in the period immediately following the end of the fixed exchange rate system, were different methods of accounting for foreign currency translation adopted by standard-setting bodies in different countries with investor-oriented approaches to financial reporting and how did the move toward harmonizing those standards evolve? Second, plausible explanations for the various choices made by these bodies over time based on the five factors in which these countries differed are discussed. This can be accomplished in a couple of ways: one, the elimination of plausible ideas by demonstrating that the truth of a situation was the opposite of, or more complex than,

commonly believed,[13] or by formulating a new hypothesis consistent with the comparative evidence[14]; two, the resolution of paradoxes by showing that plausible causal explanations appear to be surprising and then pointing to another set of causes that make the phenomenon expected after all.[15]

The empirical work for the comparative analysis entails examining the activities of the following standard-setting bodies in developing standards for foreign currency translation during the 1970s and the 1980s: the US FASB, the ASC (from 1990, the ASB) in the UK, the Australian AARF and its associated subcommittees, and the Canadian CICA. As indicated earlier, these countries have in common a similar purpose to financial reporting, the role of the state, the standard-setting process, etc., and were the most active in developing standards for foreign currency accounting. (Most European countries did not develop foreign currency standards until the 1980's with the advent of the Fourth Directive.) Because the IASC is a very heterogenous group representing many constituencies, an analysis in which tax laws are compared, for example, is not feasible. However, the inclusion of the IASC in this study of power relations is warranted because certain individuals and organizations "infiltrated" the thinking of the IASC as well.

Documents examined include minutes of meetings of the standard-setting boards

---

13 Neil J. Smelser, *Comparative Methods in the Social Sciences* (Englewood Cliffs, N. J.: Prentice-Hall, 1976).

14 William H. Sewell, Jr., "Marc Bloch and the Logic of Comparative History", *History and Theory* 6 (1967): 208-218.

15 Smelser, *ibid.*

and subcommittees pertaining to foreign currency translation, letters of comment to the boards from outside parties on issued pronouncements on foreign currency translation, newsletters and other relevant documents (to the extent available). Data gathered also includes current practices of companies at the time of developing standards in each country according to company surveys as well as currency fluctuations of each country during the period of the 1970s and 1980s and information on tax laws for each country during that time period.

Skocpol discusses inherent problems in comparative analyses, one of which is the assumption that the units being investigated are independent of each other.[16] This study emphasizes the interrelationships of the cases in the analysis on power. This approach does not invalidate the method of comparative analysis; rather this study investigates each case independently to test certain possible explanatory variables (the five factors), even if there is interdependence, and then investigates this interdependence in the analysis on power. Evidence indicates that certain standard-setting bodies waited until the outcomes in other countries manifested and that they were willing to work together to harmonize standards. Despite these actions and expressed intentions, the standard-setting bodies initially adhered to differences in certain provisions of the standards and only later did they move towards consensus.

---

16 *Ibid.*

II. A Comparison of Methods and Pronouncements on Foreign Currency Accounting

To understand developments in accounting for foreign currency since 1973 requires some knowledge of the different methods promulgated by various accounting bodies. The important issues are the method of translating balance sheet items and the treatment of resulting translation gains and losses. The controversy concerning translation of balance sheet items centres on which exchange rate to use for each item: the current rate (the exchange rate on the day that the balance sheet was prepared) or the historic rate (the exchange rate on the day the asset was acquired or the liability incurred). The controversy concerning treatment of translation gains and losses concerns recording gains and losses on the income statement (thus affecting net income and "signals" of corporate performance such as earnings-per-share [EPS]) or recording them as an adjustment to equity on the balance sheet (with no effect on net income). Each of these issues has been controversial almost since the first pronouncement was issued.

The nature of the controversy is depicted in the different effects of FAS 8 and FAS 52 issued in the US. FAS 8 was the first compulsory standard issued and it in effect restricted the choice of translation methods to the temporal method.[17] It also eliminated

---

[17] The temporal method is very similar to the monetary-nonmonetary method. The translation of monetary items is the same. Nonmonetary items carried on the balance sheet at historical cost are translated the same way. Those nonmonetary items which have been revalued (i.e., lower of cost or market, writedowns, upward revaluations) from historical cost are translated at the current rate, as opposed to the historic rate under the monetary-nonmonetary method. Translation of the income statement is basically the same as the monetary-nonmonetary method. (Choi and Mueller, *ibid.*).

the opportunity for managers to smooth earnings through deferral of unrealized gains and losses. The result of translation under FAS 8 was erratic profit margins and other ratios, making financial indicators difficult to interpret and performance difficult to compare.[18] FAS 8 forced managers to incur costs to minimize translation adjustments.[19] Surveys suggest that public accountants favoured FAS 8 but financial executives reacted negatively to the new standard, citing increased economic exposure and the concern over having to expend time and money to hedge accounting risks.[20]

FAS 52 alleviated these problems to some degree because it eliminated the problem of different ratios under different currencies that plagued FAS 8.[21] Managers reporting under FAS 52 can exercise judgment in determining the functional currency, in determining whether subsidiaries are integrated or independent (which affects treatment of gains and losses), and in determining which countries are hyperinflationary or not

---

18

William D. Serfass, Jr., "Possible Undesirable Effects of FASB No. 8," *CPA Journal* 46 (May 1976): 59; Trevor S. Harris, "Foreign Currency Transactions and Translations", in Choi, 1991, *ibid.;* Choi and Mueller, *ibid.*

19

Choi and Mueller, *ibid.*

20

Frederick D. S. Choi, Howard D. Lowe, and Reginald G. Worthley, "Accountors, Accountants, and Standard No. 8," *Journal of International Business Studies* (Fall 1978): 81-87; Marjorie T. Stanley and Stanley B. Block, "Response by United States Financial Managers to Financial Accounting Standard No.8," *Journal of International Business Studies* (Fall 1978): 89-99.

21

James A. Largay III, "SFAS No. 52: Expediency or Principle?" in Jagdish Sheth and Abdolreza Eshghi, eds., *Global Accounting Perspectives* (Cincinnati, OH: South-Western Publishing Co., 1989).

(which affects choice of translation method).[22] The improved stability of earnings enables managers to spend less resources on management of foreign exchange and reduces the incentive to hedge translation exposures.[23] The results of surveys confirm that managers believe that earnings are more stable, that fewer companies are hedging, and that a variety of techniques are being applied in choosing the functional currency. However, analysts are critical of the flexibility in choosing a functional currency and in identifying hyperinflationary economies.[24] (See Appendix III for a numerical example of the different effects of the current rate method and the temporal method.)

The standard-setters in the US, the UK, Canada, and Australia have advocated a number of different methods for translating foreign currency balances over time. The early pronouncements among these countries varied more than those in recent times. (See Table 1 for a list of pronouncements.) The US standard-setters advocated first one method, then primarily two, but pronouncements were mainly recommendations and not mandatory until FAS 8, which reduced the number of acceptable translation methods to one. By introducing the concept of a functional currency, FAS 52 permits the use of the

---

22

Current standards regarding hyperinflationary economies vary among the countries in this study. The US and Canada require the temporal method for translation of statements from subsidiaries in these economies, while the IASC, Australia, and the UK require restatement for effects of price level changes before translation using the temporal method (Kirsch and Becker-Dermer, *ibid.*).

23

Mauer, *ibid.*

24

Jerry L. Arnold and William W. Holder, *Impact of Statement 52 on Decisions Financial Reports and Attitudes* (Morristown, NJ: Financial Executives Research Foundation, 1986).

current rate method[25] and the temporal method in specified circumstances which managers can judge for themselves. The US, Canada, the UK, and Australia all eventually merged towards the use of both current rate and temporal methods. Australian standard-setters officially permitted the current rate method initially, then the temporal method, but eventually followed the rest of these countries. Canadian standard-setters permitted a number of methods initially, then followed the US example, endorsing the temporal method, and finally issued a pronouncement similar to FAS 52. The UK standards had always endorsed two acceptable methods, although SSAP 20 is more specific than earlier UK pronouncements as to when the current rate method and the temporal method should be used. The pronouncements of the IASC have mainly allowed both the current rate and temporal methods throughout. New Zealand standard-setters never endorsed the temporal method, but first recommended the current rate method and later adopted both the current rate and the monetary-nonmonetary methods. Japan, the only non-English-speaking country that has issued a number of pronouncements, has always permitted the use of more than one method.

The treatments of translation gains and losses are less variable among these countries. The US and the UK standards are the only ones that required gains and losses to be run solely through the income statement. The US pronouncements went back and forth from income statement treatment only (Bulletin 92) to some deferment (ARB 43) to

---

25

All balance sheet items are translated at the current rate as of the balance sheet date under this method. Income statement items are translated using an average rate for the year (Choi and Mueller, *ibid.*)

income statement only (FAS 8) to some deferment (FAS 52). The UK pronouncements required income statement treatment only in ED 21 but subsequent pronouncements permitted deferment. All other countries permitted some deferment, although variations exist regarding which gains and losses can be deferred. Canada's 1977 ED, issued after FAS 8 was issued in 1975, was very similar to FAS 8 except for permitting deferral of gains and losses on translation of nonmonetary items.[26] Likewise, Australia's 1979 ED endorsed the temporal method, like FAS 8, but permitted deferral of unrealized gains and losses on long-term receivables and payables.[27] UK's ED 21 was like FAS 8 on the deferment issue but permitted more than one translation method.[28] ED 27 (and subsequently SSAP 20) permitted deferment of gains and losses on translations that do not give rise to cash flows.[29] IASC's E 23 and IAS 21 and Canada's AR 1650 permit deferment for gains and losses on long-term monetary items, which FAS 52 does not.[30]

26

David A. Scott and Bryan C. Walker, "Foreign Currency Translation in Canada and the U. S.", *CA Magazine* 10 (November 1977): 48-53.

27

Australian Accounting Research Foundation, ED 11, *Proposed Statement of Accounting Standards: "Translation of Foreign Currency Transactions and Foreign Currency Financial Statements in the Context of Historical Cost Accounting"* (June 1979).

28

P. Raymond Hinton, "Foreign Currency Translation: Conceptual and Practical Limitations of the Currency Rate Method", *The Accountant* 178 (May 4, 1978): 591-592.

29

Accounting Standards Committee, *ibid.*, 1980; Accounting Standards Committee, "SSAP 20: Foreign Currency Translation", *Accountancy*, 94 (May 1983): 120-128.

30

Journal of Accountancy, "IASC Issues Second Draft on Translation", 153 (March 1982): 20; "CICA Exposes Draft on Foreign Currency Translation", 154 (August 1982c): 18; *ibid.*, 1983.

The US standards appear to be slightly less flexible than most other standards on foreign currency accounting on these issues, even with the greater flexibility offered by FAS 52 over FAS 8.

Since the 1930s, pronouncements for foreign currency accounting typically followed a currency revaluation.[31] What distinguishes the situation of the early 1970s from previous currency fluctuations is the switch to a floating exchange rate system from a fixed-rate system and the decline in the strength of the US dollar. These combined circumstances had significant implications, particularly for managers of MNCs operating primarily in US dollars and holding net liabilities in foreign currency. The efforts to establish guidelines for foreign currency accounting originated primarily in the US in the early 1970s. The early pronouncements did not alleviate problems; in fact, they created new ones. Accounting standard-setters faced an unusual situation when the floating exchange rate system went into effect. It was a set of circumstances with little or no precedent. Guidelines issued by the standard-setting bodies in the countries in this study varied on some very significant issues. These differences impeded the harmonizing of these standards for a time, but were eventually reduced to achieve a certain level of consensus and flexibility among the standards in these countries. The remainder of this chapter and this dissertation attempts to explain why these differences existed in the first place and to illustrate the social aspects of the development of the standards that are in effect today.

---

[31] Russell W. Willey, *Foreign Exchange: The Accounting, Economics, and Control* (Wilmington, DE: Nopoly Press, Inc., 1977).

III. Currency Fluctuations

Pronouncements on accounting for foreign currency translation in the past have at times followed a change in foreign exchange rates. Table 1 provides an outline of the history of pronouncements with those following a foreign exchange rate change shown in bold. In 1931, after only one month of deliberation, the American Institute of Accountants (AIA; now called the American Institute of Certified Public Accountants (AICPA)) issued an official pronouncement on accounting for foreign operations, Bulletin No. 92, entitled "Foreign Exchange Losses". It was issued in response to "the numerous and severe fluctuations [primarily losses] in foreign exchange that have occurred during the year."[32] It recommended the use of what became known as the current-noncurrent method.[33] Some of the wording of the pronouncement resembled part of a speech presented by Cecil S. Ashdown to the AIA at their annual meeting in Chicago, September, 1922.[34] But an official recommendation was not issued until

---

32

Special Committee on Accounting Procedure, American Institute of Accountants, "Foreign Exchange Losses", *Bulletin of the American Institute of Accountants,* No. 92, December 15, 1931, quoted in Willey, *ibid.*

33

Under this method, current assets and current liabilities of the foreign subsidiary are translated using the current rate as of the balance sheet date. Noncurrent assets and liabilities are translated using the historic rate. Income statement items are translated using an average rate of the reporting period, except for depreciation and amortization which are recorded at the historic rate applicable to the corresponding noncurrent assets (Kirsch and Becker-Dermer, *ibid.*).

34

Gerhard G. Mueller, "Are Traditional Foreign Exchange Translation Methods Obsolete?", *California Management Review* 7 (Summer 1965): 41-46.

fluctuations in foreign exchange rates occurred in the early 1930's.

In 1949 the Research Department of the AIA issued a statement discussing various other translation methods in addition to the current-noncurrent method. This report followed a wholesale devaluation of currencies of 25 countries and argued for charging material losses from these devaluations to retained earnings instead of income.[35]

However, accounting for foreign currency translation was not a major issue for most countries between 1944 and 1968 due to stable exchange rates established and maintained by the Bretton Woods agreement of 1944. Though recommendations by the accounting profession existed, companies used a variety of methods for translation. Officially and unofficially, a variety of methods were tolerated by authoritative bodies.

Major currency devaluations in the late 1960's and early 1970's led to hasty efforts by accounting bodies in a number of countries to independently establish some continuity and uniformity for accounting for translation of foreign account balances, at least in those countries where consolidated financial statements were required.[36] As stated in

---

[35] Bulletin 117 previously issued recommended that translation gains be deferred but that losses be realized in the current year in the income statement. Thus, only losses from devaluations would affect the income statement. The 1949 statement recommended other treatments to offset this inconsistency (Konrad Kubin, "Accounting for Foreign Currency Translations: Current Problems in Historical Perspective", *Accounting Historians Journal* 2 (1975): 11-16.)

[36] Japanese companies were not required to issue consolidated statements until 1977 (Thomas T. Yamakawa, "How the Strong Yen Influenced Financial Reporting in Japan", *Management Accounting (NAA)* 60 (June 1979): 26-31). The European Union first required consolidation in the Seventh Directive issued in 1983 (Gerhard Mueller, "1992

Chapter 1, in many countries, the parent and subsidiary companies were treated as single entities for accounting purposes. Thus, a single set of financial statements must be prepared that consolidates the financial statements of the parent and subsidiary companies. When financial statements of the foreign subsidiary are prepared in the local currency, its assets and liabilities must be translated to the parent company currency. Meaningful financial statements cannot be prepared using multiple currencies and are typically prepared using the currency of the parent company.

The Council of the Institute for Chartered Accountants in England and Wales (ICAEW) issued an official recommendation on foreign currency accounting (No. 25) in 1968, a few months after the devaluation of sterling the previous year.[37] In February, 1970, the Philippine peso was allowed to float to a free market rate which resulted in a drop of almost 50% against the US dollar, the largest devaluation of a currency after World War II. "Acting with a speed rarely seen in professional accounting organizations,

---

and Harmonization Efforts in the EC", in Choi, *ibid.*, 1991). German law did not require companies to consolidate foreign operations until 1990, but only disclosure of translation method used is required (Harris, *ibid.*) Before 1965, no consolidation was required in Germany. From 1965 to 1990, German companies had to consolidate only domestic subsidiaries (R. H. Parker, "Principles and Practice in Translating Foreign Currencies: An Essay in Comparative Accounting", 6 *Abacus* (December 1970): 144-153). Similarly, the Netherlands does not have rules concerning foreign currency accounting. Danish accounting law required consolidation beginning in 1981, but does not prescribe a method for translating foreign account balances (Choi and Mueller, *ibid.*). Hence, these countries did not issue pronouncements on accounting for foreign currency until much later.

37

Parker, *ibid.* Sterling was devalued on November 18, 1967. The Council formed a subcommittee to draft guidelines for practice on November 29, 1967. (From minutes of the Technical Committee of the Council of the ICAEW, December 21, 1967.)

in March 1970 the Philippine Institute of Certified Public Accountants issued a Special Bulletin, No. 1/70, Accounting for the Effects of the Foreign Exchange Rate".[38] Similarly, in Japan, Opinions 3, 4, and 5 followed a revaluation of the yen in 1971.[39] In the US, the Accounting Principles Board's (APB) 1971 ED followed the US decision to prohibit the conversion of US dollars into gold.[40] Exposure Drafts in the US, Mexico, and Australia, and Opinion 6 in Japan issued in 1973 came in the wake of floating exchange rates.

The following quote from FAS 8 describes the accounting effects of a weakening dollar:

> As long as most foreign currencies weakened against the dollar, as they usually did...until about 1969, translating inventory at the current rate and long-term debt at historical rates under current-noncurrent method probably produced conservative results....Once the dollar began to weaken against foreign currencies, however, that translation method lost its conservative appeal because it produced the opposite results.[41]

This statement from FAS 8 implies that choice of translation method for foreign currency accounting could depend on the relative strength of the currency. If the domestic

---

38

Lee J. Seidler, " An Income Approach to the Translation of Foreign Currency Financial Statements", *The CPA Journal* 42 (January 1972): 26-35.

39

Yamakawa, *ibid.*

40

Willey, *ibid.*; Choi and Mueller, *ibid.*

41

FASB, *Statement of Financial Accounting Standards No. 8: Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements*, (Stamford, CT.: Financial Accounting Standards Board, October, 1975): para. 125.

currency devalued relative to other currencies and the accounting results changed, it could be argued that the standard-setting body would be pressured to change the accounting rules. This section investigates the possibility that the choice of translation method and treatment of gains and losses coincided with or offset any negative accounting effects of currency fluctuations.

Evidence suggests that new pronouncements on foreign currency accounting issued by the FASB did indeed follow a devaluation of the US dollar. FAS 8 was in various stages of development from 1973 to 1975, a relatively volatile time for the US dollar which generally devalued from pre-1970 levels. From December 1971 to March 1973 the US dollar devalued cumulatively about 15% from parity levels set in 1970[42] (see Appendix II for a chart of effective exchange rates from 1973 to 1979).[43] The FASB placed foreign currency translation on its first agenda in April, 1973, and issued FAS 1 on disclosure for foreign currency translations in October, 1973, with the stipulation that a more extensive statement would be issued in the future. From November, 1973, through February 1975, the dollar rose, then dropped, and then dropped some more. The ED that was the precursor to FAS 8 was issued in December, 1974, and FAS 8 was issued in October, 1975. The quote from FAS 8 suggests that the weakening of the dollar prompted the change in accounting standards to prohibit the use of methods that produced less-than-conservative results. In 1978 the dollar fell a total of 13% points,

---

42 *OECD Economic Outlook*, July, 1973.

43 *Ibid.*, December, 1979.

then for the most part remained at these levels until the end of the decade and after FAS 52 was issued.

When the dollar weakened in 1977 and 1978, FAS 8 was criticized as being "conceptually unsound".[44] The new standard, FAS 52, issued in 1981, did not prohibit the use of the temporal method, but restricted its use to specific cases, and endorsed the current rate method as an acceptable method. If the temporal method required by FAS 8 was to eliminate the problems associated with the current-noncurrent method due to dollar devaluation, it is not likely that further devaluation would result in the temporal method "falling out of favour" with standard-setters or constituents. The accounting effects should remain the same. Although the condition of a devaluing dollar may have had an influence on the FASB's decision to endorse the temporal method in the early 1970s, in view of further dollar devaluation in the 1970s, the FASB's decision to endorse the current rate method was likely based on other factors. One of the reasons for criticizing the temporal method was the income statement treatment of gains and losses required by FAS 8 which resulted in profit fluctuations not due to operations. This effect was more likely the reason for the endorsement of the current rate method.

From December 1971 to March 1973, sterling fell 12 percentage points from the levels of the Smithsonian agreement.[45] It fell steadily until mid-1975, preceding the

---

[44] James Carty, "Foreign Currency Translation and Hedging", Technical Weeks paper, November, 1995. See also Appendix 2 of ED 27.

[45] *OECD Economic Outlook*, July, 1973.

issuance of ED 16. In 1976 sterling fell an additional 16 percentage points, preceding the issuance of ED 21. Sterling fluctuated in 1978 and 1979, with its greatest drop against the dollar occurring during 1975-76 and then rebounding somewhat by the end of the decade (see Appendix II).

As in the US, if the temporal method had created problems when the domestic currency was devaluing, then it would not have made sense to endorse the temporal method in the UK, even under specific circumstances, while sterling was continually falling. The income statement treatment for gains and losses was also prevalent in the UK standards. However, in the UK, the current rate method permitted the offset of exchange losses on liabilities to gains in fixed assets under the cover approach, which was not permitted under the temporal method. This difference may account for the tolerance of the income statement treatment of gains and losses in the UK. FAS 52 permits some offsetting, but the offsetting gains and losses have to be in the same currency, while SSAP 20 does not require that the offsets be in the same currency.

While both the US and the UK suffered from devaluing currencies during the 1970s, these countries differed in other ways which may have influenced the choice of accounting methods. The amount of exports and imports by UK companies as a percentage of gross domestic product (GDP) was considerably higher than that of US companies during the same time periods. Exports and imports for US companies from 1971-75 were each 7% of GDP compared to 26% and 27%, respectively, for the UK.[46] A

---

[46] From OECD, *National Accounts and CSO*, cited in James Carty, "Accounting for Foreign Operations", paper for discussion at ASC meeting, November 14, 1979.

relatively lower percentage of foreign operations would suggest that exchange gains and losses would not affect profits to the degree that would be found in the UK. The UK also experienced a higher level of inflation during the early 1970s than did the US. US inflation reached double digits only by the late 1970s. A comparatively lower rate of inflation in the US allowed the US to maintain the historical cost concept of the temporal method without the problems that inflation would create (see Appendix III for an example of the effects of inflation). Thus, the temporal method (with its income statement treatment of translation gains and losses) could be tolerated until exchange gains and losses became material items as foreign operations increased for US companies, or until inflation created translation problems that could be alleviated by adopting the current rate method.[47] Furthermore, the US is one of the few countries in the world that will not allow upward revaluations of assets, while the UK does.[48]

Currency devaluations combined with high inflation rates to some extent can explain the preference for the current rate method in the US and the UK. These two countries both experienced devaluing currencies at the same time. The temporal method was criticized as an acceptable method while currencies were devaluing, yet the FASB may not have perceived the difficulties that the temporal method creates in times of devaluing currency. It was the devaluing currency combined with inflation, also

---

47

Carty, *ibid.*, 1979.

48

The US eventually addressed the issue of changing price levels as they affect foreign currency translation in FAS 33.

influenced by the percentage of GDP from foreign operations and other accounting policies concerning asset revaluation.

The Australian dollar behaved quite the opposite of the US dollar and UK sterling, at least during 1973, during which time it rose a total of 11% relative to the Smithsonian parity levels. As the data in Appendix II indicates, it fluctuated considerably during 1974. At the end of 1976 it plunged 17% in the month of December and dropped further during 1978.[49]

The effect of the strengthening dollar in 1973 was a gain on foreign debt for Australian companies.[50] When the dollar subsequently devalued and losses were incurred,[51] the deferral method of treating gains and losses on long-term monetary items would be favoured by companies, for although the losses still ran through the income statement, they were extended over the life of the liability and there was a chance that the dollar would recover and reverse the losses. However, the reserve method, which was used by companies in practice, would eliminate any effect on income because the gains and losses are taken to the equity section of the balance sheet. The reserve treatment was not allowed until 1983 with the adoption of the current rate method in ED 24. The deferral treatment for long-term liabilities in Australian standards did not coincide with

---

[49] *OECD Economic Outlook*, December, 1979.

[50] The Australian Financial Review reported gains of $9.2 million for Bougainville Mining Ltd. in 1972 and $6.5 million for Lombard Australia Ltd. in 1973.

[51] $1.6 million loss for Ciba-Geigy Australia in 1975, $20 million for BHP and $987,000 for Lombard in 1977 (The Australian Financial Review, 1975 and 1977).

the treatments in FAS 52 and SSAP 20 which required that gains and losses be reported on the current year's income statement. The US and UK standards incorporated the offsets of the liabilities with fixed assets to deal with the unfavourable losses in long-term liabilities under the current rate method (but with more restrictions in the US). Ultimately, in SSAP 20, FAS 52, and ED 24, the current rate method with its reserve treatment was the method endorsed by standard-setting bodies (except in hyperinflationary economies). It gave a favourable option to companies that had long-term debt in foreign currency, which, under the functional currency approach in FAS 52, permitted the use of the current rate method and the reserve treatment.

However, the question is again raised concerning the choice of the temporal method by the Australian standard-setters in 1979 when the Australian dollar had been devalued, creating losses on debt in foreign currency. The deferral treatment offset some of the difficulties of the temporal method by not reporting these losses on the current year's income statement, but only if the domestic currency recovered. Without recovery, the losses would show up when the liability was settled. The Australian dollar continued to fall in the 1980s.[52] The effects of the deferral method were brought to light when Alcan Australia wrote off $69 million in unamortized foreign exchange losses in 1985.[53] If the standard-setters were truly following the lead of the US and the UK, why did they not adopt the offset provision for long-term liabilities? Ultimately, in 1987 with the

---

[52] *OECD Economic Outlook*, 1989.

[53] *Business Review Weekly*, 1986, p. 125.

amended AAS 20 and ASRB 1012, the deferral method was disallowed. All three countries discussed so far experienced a devalued currency, yet the treatment of gains and losses on long-term monetary items differed among them. As with the US and the UK, the choice of methods and treatments for foreign currency accounting in Australia were the result of factors that may include a devaluing currency but these choices cannot be fully attributed to currency fluctuations.

The Canadian dollar was revalued twice in the early 1970s before floating exchange rates, first in 1970, and then in 1972. With the advent of floating exchange rates, the Canadian dollar fell steadily in the first half of 1973 but not with the severity of the US dollar and sterling (a total of 8% from Smithsonian parity levels). From late 1974 to late 1976, the Canadian dollar was quite volatile but not with the sharp drops experienced by the Australian dollar. Thereafter, the Canadian dollar fell rather steadily throughout 1977 (a drop of 10%) and 1978 (a further drop of 17%).[54]

It was during those last two years that the CICA issued its first drafts of a recommendation for foreign currency accounting in Canada. Similar questions as those raised in the Australian case can be raised concerning the choice of the temporal method for the translation method. At the time, Canada was heavily dependent on foreign capital markets. In the first half of 1976, 47% of new security issues were in foreign currency, up from 26% in the previous year.[55] With a devaluing currency which created losses on

---

[54] *OECD Economic Outlook*, December, 1979.

[55] John S. McCallum, "Foreign Currency Borrowing: The Canadian Perspective", *CGA*

foreign debt, why would the CICA endorse the temporal method with the deferral treatment of gains and losses on foreign borrowings? Without recovery of the domestic currency, the losses would show up when the liability was settled, which creates the possibility for huge write-offs on foreign exchange losses. If the standard-setters were not following the lead of the US, why did they not adopt the offset provision for long-term liabilities that was adopted in the UK? The 1978 ED rejected this approach on the grounds that: "Such an offset does not recognize the fact that the timing of the inflow of monetary assets does not necessarily correspond with the outflow to settle monetary liabilities."[56]

In the UK, it could be argued, the current rate method and the reserve treatment was preferred because of the problems of inflation, as indicated earlier. In the US, inflation was relatively low at the time that FAS 8 was issued but inflation rates increased later, so it could be argued that the US standard-setters were not pressured to change FAS 8 until the problems of inflation became prevalent. However, that argument fails to explain the Canadian case. In a period of an undervalued currency, imports become more expensive and, in the short run, keeps the inflation rate up. In 1974 and 1975, Canada experienced higher inflation rates relative to other countries including the US. The government responded with a monetary policy that resulted in higher interest rates. This led to increased foreign borrowing by Canadian corporations and

---

Magazine (April 1977): 3-6.

[56] CICA, "Translation of foreign currency transactions and foreign currency financial statements", *CICA Handbook* Section 1650, 1978, para. 1650.45.

municipalities and the process of converting the foreign funds into Canadian dollars resulted in an increase in the Canadian dollar relative to the US dollar (hence the 11% increase in 1975 and 1976). The Canadian dollar fell by November of 1976, as a result of a uncertainty after an election and a drop in interest rates, setting the stage for inflation rates to increase.[57]

Inflation in Canada was prevalent before the accounting standards were issued. According to the previous argument concerning the effects of the temporal method when the domestic country is experiencing inflation, the CICA should not have endorsed the temporal method when Canada was experiencing a period of inflation and a devaluing currency. As with the Australian case, it does make sense to adopt a deferral treatment as opposed to immediate recognition when there are losses on foreign debt, but it does not make sense to adopt the temporal method in lieu of the current rate method with a reserve treatment which would have avoided the possibility for huge write-offs as those experienced in Australia. Had the devaluing currency and the effects of inflation played a major role in the decisions of the standard-setters in developing standards for foreign currency, it seems unlikely that they would have made the choices they did. The currencies of the UK, Australia, and Canada all fell steadily relative to the US dollar in the 1980s (see table R 21 in Appendix II). Perhaps by this time, standard-setters were pressured by companies and investors to adopt the current rate method and the reserve treatment to avoid the income statement effects of losses on foreign currency borrowings.

---

[57] McCallum, *ibid.*

The actions and decisions by standard-setting bodies in the US, the UK, Australia, and Canada are not consistent with the effects of the devalued currencies in each country. The currency devaluations combined with high inflation and a high percentage of imports and exports provide some support for the preference of the current rate method but not for the temporal method. The consensus that eventually developed among these countries and the IASC can hardly be attributed to the effects of currency devaluations. The current rate method would be preferred only if currency devaluations coincided with these other conditions in all of these countries at the same time, which they did not.

Furthermore, the logical inconsistency between currency devaluations and the treatment of gains and losses may be evidence of the fact that the effects of currency devaluations are not uniform among countries at any point in time or even, perhaps, over time for the same country. Because currencies may or may not fluctuate in tandem with each other, it hardly seems likely that consensus developed as a response to currency devaluations in these countries.

The evidence suggests that a weakening domestic currency could affect companies' results of operations and that standard-setters could be sensitive to any negative results that a weakened currency would create. Their choices of translation method and treatment of gains and losses then might be affected by currency fluctuations and might explain the differences in these choices. This argument assumes that all companies would be affected the same way when domestic currency devalues. If that be the case, companies affected by currency devaluations would have an incentive to influence the development of standards for foreign currency accounting. A pluralist view

of power would suggest that the lobbying process by interested parties would result in these interested parties affecting the decisions made by standard-setting bodies. That is one of the subjects of the next chapter.

IV. Conclusion

Circumstances and events in accounting history suggest that accounting for foreign currency translation developed in response to currency devaluations. Many of the early pronouncements arose from a change in domestic currency. The demand for information on foreign currency gains and losses skyrocketed when exchange rates suddenly began to fluctuate on a daily basis with the dismantling of the fixed exchange rate system in 1973. The demand for accounting information coupled with the necessity of managers to hedge against accounting risks prompted standard-setting bodies to initiate hasty action in developing guidelines for foreign currency accounting.

In this chapter, the Method of Difference applied to currency fluctuations indicates some preference for the current rate method when domestic currency devalues, if other extenuating circumstances are also present. However, for that argument to hold, the choices for translation method made by standard-setters in Canada would have followed those in the US and the UK, which they did not. Also, the analysis indicates that the deferral method is a logical choice when domestic currency devalues but that was not the choice of standard-setters in the US and the UK. The inconsistencies between currency devaluations and the choices made by standard-setting bodies have

already been discussed and will not be repeated. The different choices made by standard-setters in the early standards as well as the consensus that followed can be attributed only partially to the relative strength of the domestic currency because the effects of a devalued currency would not be uniform among countries or MNCs. Results of the analysis provide some support for the effects of currency fluctuations on choice of translation method, but only in light of certain other circumstances and not consistently from country to country, and very little evidence of causality between currency fluctuations and choice of treatments for gains and losses. The discussion at the end of the next chapter explores the possibility of interaction effects due to relationships among the factors themselves.

Table 1. Pronouncements on Accounting for Foreign Currency Translations and Transactions*

Year	US	Mexico	Canada	UK	Australia	New Zealand	India	Japan	Philippines	IASC
1931	**Bull.92**									
1933	Bull.117									
1939	**ARB4**									
1941	**AIA ST.**									
1949	**AIA ST.**									
1953	ARB43									
1960	NAA 36									
1965	APBO6									
1968				**ICAEW25**						
1970									**Bull.1/70**	
1971	**APB ED**							**OP.3,4**		
1972	ARS 12							**OP.5**		
1973	**FASB ED** **FAS 1**	**ED**			**ED**			**OP.6**		
1974	FASB ED									
1975	FAS 8			ED16						
1976	INT.15						ICAI ST.			
1977	INT.17 ED (8)		ED	ED21						E11
1979					ED			STD		
1980	FASB ED			ED27		TPA2				
1981	ED (REV.) FAS 52									
1982			ED	SSAP20						
1983			AR1650		ED					IAS 21
1985					ASRB1003 AAS20					
1986						ED37				
1987					ASRB1012 AAS20 (A)	ED37A				
1988						SSAP21				

Table 1.(cont.) Pronouncements on Accounting for Foreign Currency Translations and Transactions*

Year	US	Mexico	Canada	UK	Australia	New Zealand	India	Japan	Philippines	IASC
1989							INT 17			E32
1992										E44

* Boldface indicates that these pronouncements followed a change in domestic currency

Bull. = Bulletin
ARB = Accounting Research Bulletin
AIA = American Institute of Accountants
ST = Statement
NAA = National Association of Accountants
APBO = Accounting Principles Board Opinion
ICAEW = Institute of Chartered Accountants in England and Wales
ED = Exposure Draft
OP = Opinion
FASB = Financial Accounting Standards Board
FAS = Financial Accounting Standard
INT = Interpretation
ICAI = Institute of Chartered Accountants of India
E = Exposure Draft
STD = Standard
ED (8) = Exposure Draft to amending FAS 8
TPA = Technical Practice Aid
REV = Revised
SSAP = Statement of Standard Accounting Practice
AR = Accounting Recommendation
IAS = International Accounting Standard
ASRB = Accounting Standards Research Board
AAS = Australia Accounting Standard

CHAPTER 3. A COMPARATIVE HISTORY OF ACCOUNTING FOR FOREIGN CURRENCY TRANSLATION

The purpose of this chapter is to continue the comparative analysis of choices made by standard-setting bodies in the US, the UK, Australia, and Canada to show the extent that other factors might have influenced these choices. In the preceding chapter, the possibility that accounting standards may have been changed to offset the effects of a weakening domestic currency (assuming that the majority of companies with foreign operations were adversely affected by it) was examined. This chapter examines whether the extant current practice and the application of accounting principles that existed prior to the interest in foreign currency accounting may have influenced the standards adopted in each country. Recognizing the political nature of the standard-setting process, this chapter also builds on previous research that has investigated lobbying efforts towards standards for foreign currency accounting. Finally, this chapter also examines the extant tax laws on realized and unrealized gains and losses and their possible effects on financial reporting standards for foreign currency gains and losses.

Several references have been made in journal articles and other documentation to then existing practices in accounting in each country influencing foreign currency differences. Current practices are described in publications by standard-setting bodies and other organizations.[1] Some of the comments noted that in some areas, standards

---

[1] Financial Accounting Standards Board, *FASB Discussion Memorandum: An Analysis of Issues Related to Accounting for Foreign Currency Translation* (Stamford, CT: FASB) February 21, 1974; Christina S. R. Drummond, C. A., *Foreign Currency Translation* (Toronto: Butterworths) 1983.

differed significantly from current practice.[2] But in at least one case, the intent was to follow current practice: "the disposition of exchange differences arising from use of the current method is to be in accordance with predominant practice...."[3] In another case, it was also implied that current practice should be followed:

> Theory and practice in North America support the view that fixed assets should be translated at historic rates of exchange.....the historic rate method is so widely accepted in practice, that a Canadian company that today translated the fixed assets of a foreign branch or subsidiary at the current exchange rate....could regard itself as pioneering a new accounting method in Canada.[4]

In the UK, it was believed that the standards did indeed follow current practice: "ED 27 will affect the foreign exchange management practices of UK companies, but not significantly. More than 90% of major UK companies already use the closing rate

---

2

Fantl, *ibid.*; Mauer, *ibid*; Accounting Standards Committee, *ibid*, 1980.

3

Letter from K. M. Stevenson, Technical Director of the AARF, to Mr. Ian Philip, partner at Price Waterhouse & Co., commissioned to develop an exposure draft on foreign currency accounting in Australia, December 18, 1979. Mr. Philip responded to Mr. Stevenson concerning, among other things, his views on the divergence in practice on handling gains and losses on translation and that due to this range in practice it would be dangerous to use a survey of current practice as a basis for formulating a standard (Letter to Mr. Stevenson, dated February 11, 1980).

4

R. MacDonald Parkinson, FCA, "The Floating Dollar", *Canadian Chartered Accountant* (January 1971): 59-63.

method so that only the treatment of exchange differences will be changed."[5] Certainly the use of current foreign currency practices as a basis for developing standards varied from one country to another and differed between methods and other provisions. The issue this chapter is to examine is the extent to which standards for foreign currency resembled current practices.

Just as FAS 8 was criticized for deviating from current practice, it was also criticized for violating the accounting principles of conservatism and realization.[6] These concepts were discussed by the FASB along with the all-inclusive income concept in the development of FAS 8.[7] The all-inclusive concept was considered elsewhere also: "The only basis for accounting for transactions in foreign currencies (e.g. foreign borrowings) and for translating the accounts of foreign entities which can be consistently applied and which does not require a departure from the concept of an all-inclusive income statement is the current/noncurrent method."[8] At the same time, a reliance on theoretical assumptions was not favoured: "the FASB's new willingness to listen more attentively to members of the business community is a promising indication that the new pronouncement will be based on practical and realistic considerations--rather than on

---

5

Portington, *ibid.*

6

Fantl, *ibid.*

7

Financial Accounting Standards Board, *ibid.*

8

Notes for John Hepworth from I. R. Philip from the AARF files, November 3, 1976. Mr. Stevenson of the AARF was not in favour of relying on this concept (Memorandum to the AARF Executive Committee, February 2, 1980).

theoretical assumptions."[9] The use of historical rates for translation was considered consistent with the historical cost basis of accounting[10] but was not favoured by some as a basis for foreign currency translation.[11] "Standard setters are constrained by the need to operate within generally accepted accounting principles (GAAP), that is, within the historical-cost model framework, with all its deficiencies."[12] The "going concern" concept was used to justify amortization of translation gains and losses: "A basic tenet of financial statement preparation is the 'going concern' concept. The recognition of translation gains and losses breaks this concept in the respect that it forces an income effect on the translation process which is not caused by operational transactions."[13]

The use of accounting principles as a basis for determining the differences among standards for foreign currency is the focus of the examination in the next section of this chapter. Certain accounting principles appear to have been controversial at times during the development of these standards. This examination attempts to determine the extent to which different standard-setting bodies chose to adhere to different principles as a

---

9

Fantl, *ibid.*

10

David J. Moore, "Foreign Currency Translation", *CA Magazine* (September 1977): 63-66.

11

Joel H. Amernic and Brian J. B. Galvin, "Foreign Currency Translation: The Debate Goes On", *CA Magazine* (March 1982): 30-37.

12

Ibid.

13

Serfoss, *ibid.*

possible explanation for the choices that were made.

Lobbying efforts have been the focus of research studies from time to time in accounting literature,[14] with a strong emphasis on comment (or submission) letters. What is of interest in this study is the association between majority views expressed in comment letters and the choices made by standard-setting bodies in their respective countries. If the differences are due to differences in opinion of the respondents, then the question would be why do respondents differ in their opinions. But that is beyond the scope of this study. The point here is to follow up on a previous study of FAS 8 concerning lobbying activities and the final provisions of an accounting standard.[15] Although that paper suggests very little association between comments made by respondents and the outcomes of decisions made by the FASB in developing FAS 8, the question remains whether that was the case with standards in other countries. If so, then that may explain the divergence in the standards issued by the countries in this study. This is the focus of section III of this chapter.

An argument for investigating the effects of tax laws is somewhat dubious in the sense that the main issue initially was not whether gains or losses on foreign exchange are taxable, but rather it was a question of intraperiod tax allocation if deferral methods

---

[14] For example, see Lauren Kelly, "Corporate Management Lobbying on FAS No. 8: Some Further Evidence", *Journal of Accounting Research* 23 (Autumn 1985): 619-632.

[15] Bryant, *ibid.*

for these gains and losses were adopted.[16] However, in 1979 the Tax Court in the US involving The Hoover Company "held that forward contracts for the sale of foreign currency gave rise to capital gain or loss rather than to ordinary income or an ordinary deduction. This holding may affect the use of foreign exchange contracts to avoid economic exposure and accounting exposure from foreign currency movements."[17] Considering that this court decision occurred during the time that FAS 8 was under criticism for forcing corporate managers to engage in hedging and other practices to offset undesirable effects of accounting gains and losses, it would suggest that tax effects of translation gains and losses would be less important to corporate managers after this decision (because capital gains were taxed at a lower rate than ordinary income). Therefore, the tax consequences of FAS 8 before the court ruling might motivate the lobbying against FAS 8. Also, in the UK, the Chancellor of the Exchequer stated, "I have received many representations that the extra cost to companies of repaying foreign currency loans when sterling has fallen in value should rank for tax relief."[18] A committee of the professional accounting bodies in the UK also lobbied for favourable

---

16

See FASB, *ibid,* February 21, 1974 and CICA Accounting Research Committee, *Foreign Currency Translation,* Exposure Draft, June 1982, for more thorough discussions of this matter.

17

Harold S. Peckron, "Tax Consequences of Currency Futures After *Hoover*", *International Tax Journal* 6 (1980): 165-177.

18

Quoted in "Borrowings in Foreign Currency", issued by the Board of Inland Revenue, October 1976. The issue of whether translation gains and losses are of a capital nature was also discussed by the Inland Revenue in this document.

tax treatment: "The exchange risk factor is a heavy enough risk for business to bear without being exacerbated by an arbitrary and asymmetrical tax treatment of losses and profits."[19] Without prior knowledge of tax laws in these countries and their possible effects on accounting standard-setting, it became of interest to this author to investigate the possible association between the tax treatments for foreign currency gains and losses in each of these countries.

The statement made by the UK Chancellor of the Exchequer suggests that tax issues arose when sterling devalued, indicating a correlation between these events which may have a combined effect on the decisions made by standard-setting bodies. These events jointly may have motivated some of the lobbying activity in the US and perhaps the UK. The examination of these five factors is a model of association between these factors combined (somewhat as in a multiple regression). They are examined separately in chapters two and three initially, with an analysis that follows in which the combined effects are taken into account. It is shown that this combined model of factors does not explain all the outcomes of developing accounting standards for foreign currency, but it is noted in what areas the outcomes may be attributed to one or more of these factors.

The strategy used to explain the outcomes of standards-setting for foreign currency accounting of this and the preceding chapters follows that of one of Toqueville's rhetorical strategies. The strategy begins with statements of plausible views and follows with demonstrations of factual material that suggest that the truth was in fact

---

[19] Consultative Committee of Accountancy Bodies, "Borrowings in Foreign Currency", TR 209, memorandum submitted to the Board of Inland Revenue, December 1976.

opposite of, or at least more complex, than commonly believed.[20] Part I reports the study of extant practices for foreign currency accounting in the US, the UK, Canada, and Australia as a possible explanation for the choices made the standard-setting bodies in these countries. Part II reports the analysis of accounting principles as the basis for the methods of translation and treatment of gains and losses chosen by standard-setting bodies. Part III examines the effects of lobbying efforts on the development of foreign currency standards. Part IV attempts to determine any association between tax laws and financial reporting standards for foreign currency gains and losses. Part V summarizes the conclusions from this analysis in terms of the extent to which these five factors combined explain the choices made by standard-setting bodies.

I. Current Practice Argument

This section presents an examination of the current practices of foreign currency accounting prior to and at the time that standard-setting bodies issued official pronouncements on foreign currency accounting. The purpose is to determine whether differences in the early pronouncements were due to current practices in the US, the UK, Canada, and Australia and whether current practices may have contributed to the consensus that followed. My evidence suggests that accounting standards for foreign currency did reflect current practice, but only to a limited degree.

---

[20] Smelser, *ibid.*

In the US, surveys conducted by the FASB and the Financial Executives Institute (FEI)[21] report some diversity concerning translation methods. According to the FASB survey, 49 out of 77 companies disclosed that long-term payables and/or receivables were translated using current rates. All other companies used a variety of methods. (The survey did not ask about inventory). The FEI survey reported that current practice leaned towards using the current rate for translation. However, nearly all of the 45 companies surveyed translated inventory at the current rate, which is consistent with the current/noncurrent method, but translated long-term debt also at the current rate, which is consistent with the monetary/nonmonetary method. Both of these methods were accepted in the US by standard-setting bodies in the late 1970's, but it appears that companies used a mixture of the two methods. In addition, most companies (35 out of 45) used a current rate for deferrals and reserves, a practice which does not match with either method. Although several methods were recommended prior to the 1970s in the US, company practice did not follow the recommendations by standard-setting bodies. The fact that rules were to become mandatory standards, rather than mere recommendations, might explain the concern that MNCs would have over the change in the rules in the mid-1970s.

The practices of reporting of gains and losses were quite diverse. According to

---

21 Financial Accounting Standards Board, Research Staff, "A Study of Disclosure of Foreign Currency Translation Information" (December 1973); Financial Executives Institute, Committee on Corporate Reporting, Foreign Exchange Conversions Subcommittee, "Survey of U.S. Company Foreign Translation Practices" (October 31, 1973).

the FASB survey, 34 out of 69 companies that disclosed the policy concerning disposition of gains and losses reported some form of deferral. The other 25 companies recognized in full all gains and losses in the income statement. The FEI survey reported similar results. Roughly one-half of the surveyed companies (23) accounted for the gains and losses currently in the income statement and the other 22 companies deferred the gains and losses over the life of an asset or long-term debt or were taken to a reserve account. Current practice was rather mixed regarding the handling of gains and losses.

The FASB's initial pronouncement (FAS 1) on foreign currency translations required disclosure of practice without prescribing a particular method. FAS 8 prescribed the temporal method, which required that cash, receivables, payables, long-term debt, and any revaluations be translated using the current rate, while fixed assets, long-term investments, and inventories were to be translated at historic rates. The handling of receivables, payables, long-term debt, fixed assets, and long-term-investments agreed with then current practice, but the translating of inventory at historic rates disagreed with current practice, according to the FEI survey. FAS 8 also required that all gains and losses be accounted for currently in the income statement, which agreed with about one-half of the survey respondents. Given the diverse practice in handling gains and losses, the FASB could not be merely following current practice if it prescribed just one method, which it did in FAS 8. Regarding translation methods, the temporal method prescribed historic rates for inventory, which clearly disagreed with practice. While certain provisions of the FASB pronouncement agreed with practice, clearly there were provisions that did not. Thus, method choice in the US was based on

something other than current practice.

Sterling was devalued on November 18, 1967, resulting in a ICAEW draft statement of guidance concerning accounting problems of conversion of overseas currencies.[22] Recommendation N25, *The Accounting Treatment of Major Changes in the Sterling Parity of Overseas Currencies,* was issued in February, 1968, and was the first pronouncement by the UK profession concerning foreign currency accounting. Recommendation N25 dealt mainly with the reporting of the exceptional gains and losses brought about by the sterling devaluation which should be reported on the profit and loss statement as extraordinary gains and losses. Unlike the US, there was little history of issued recommendations in the UK prior to the early 1970s.

Then current practice among UK companies revealed a preference for the current rate method during the 1970s and early 1980s. In the early 1970s, roughly 90% of the UK surveyed companies that reported a translation method used the current rate method and that figure increased from 1976 onwards. ED 21, issued in 1977, endorsed both the current rate and temporal methods.[23] Comments on ED 21 reflected the opinion that two methods should not be allowed when the current rate method was so widely used in the UK.[24] Recognizing the widespread use of the current rate method in the UK, ED 27 and SSAP 20, although not requiring the use of the temporal method specifically, do specify

---

22
From minutes of meeting of ICAEW Technical Committee held on December 21, 1967.

23
Wallace and Ogle, *ibid.*

24
From comment letters on ED 21.

certain conditions to consider that might require the use of the temporal method when choosing a translation method.[25]

UK standards also differed from practice concerning the treatment of exchange gains and losses. Prior to 1975, the majority of UK companies treated these as movements on reserves. ED 16 and subsequent pronouncements required certain gains and losses to be taken to the profit and loss statement and others to be taken to reserves. Company practice shifted after the issuance of ED 16 in 1975 in that more companies were reporting gains and losses in both reserves and the profit and loss statement and fewer were taking these losses to reserves only.[26]

UK practice was less influenced by official pronouncements prior to the 1970s than US practice. US practice showed much more diversity in translation methods, possibly as a result of the APB allowing more that one method. The concern here is not, however, with how practice reflected official pronouncements, but, rather, with how pronouncements reflected or perhaps were influenced by current practice. In the case of the US with its diversity of translation methods, any pronouncement that endorsed a single method could not possibly reflect practice, which was exactly the case with FAS 8. In the UK the opposite situation occurred. UK companies reported less diversity of practice and yet the official pronouncements of the UK endorsed two methods, without even being specific about their application. In a sense, the UK pronouncements were

---

25 Wallace and Ogle, *ibid.*

26 *Ibid.*

much more liberal by virtue of the fact that the current practice was endorsed but another practice (common to the US) was also permitted, but left it up to the companies to decide which method to use. Only consistency of methods from one year to the next was emphasized. Thus, UK standards reflected UK practice, but also accommodated US rules for the benefit of UK companies that were subsidiaries of US MNCs[27] and for those US MNCs raising capital on the ever-growing Eurodollar markets of the 1970s and 1980s.

In Australia, the first ED issued in 1973 on foreign currency accounting was consistent with current practice in the translation method and in the treatment of gains and losses on translation. A survey was conducted of the 1975 or 1976 annual reports of 100 listed Australian companies known to have foreign currency transactions.[28] The number of companies out of these 100 with foreign-based operations was 73 and of these, 65 (89%) used the current rate method to translate foreign assets and liabilities. 50 out of these 73 companies included the gains and losses in the profit and loss statement. The 1973 Australian ED endorsed the current rate method and the income statement treatment of gains and losses, so either the ED reflected practice or practice was following the recommendations in the ED. This practice was also consistent with Clause 10 of the Ninth Schedule of the Companies Act which stated:

27

From an interview with James Carty, May 9, 1996.

28

W. J. Kenley, "Points from Published Accounts. Reporting of Foreign Currency Transactions", *The Chartered Accountant in Australia* (March 1978): 38-43.

All amounts shown in the accounts or group accounts shall be expressed in Australian currency, and where any conversion has been made otherwise than on the basis of the rate of exchange current at the end of the financial year of the company or holding company an explanation of the methods used in calculating the conversion shall be given.[29]

The 1979 ED endorsed the temporal method as the preferred method, clearly not reflecting the current practice in Australia. Presumably this change in preferred translation method reflects a desire to harmonize with FAS 8 in the US. However, by 1979 the temporal method was criticized by financial executives[30] and FAS 8 was under consideration for revision by the FASB,[31] so it is not clear why the AARF chose to endorse the controversial temporal method in 1979. The 1979 ED continued to endorse the income statement treatment for unrealized translation gains and losses, but, unlike the 1973 ED, made an exception for these gains and losses on long-term receivables and payables which should be amortized over the period between the movement in the exchange rate and the settlement date (i.e., over the remaining life of the receivable or payable). The survey revealed that roughly one-third of the companies surveyed treated these gains and losses in a reserve account which is not the same as amortizing the gains and losses over the remaining life of the asset or liability. The latter approach involves the income statement, the former involves only the balance sheet. The 1979 ED did not

---

29

Ibid.

30

Choi, Lowe, and Worthley, *ibid.*, and Stanley and Block, *ibid.*

31

Dennis Beresford, and D. Neary, "FASB slates major changes to statement No. 8", *Financial Executive* 47 (September 1979): 6.

reflect practice on this provision of treating translation gains and losses.

The 1983 Australian ED and AAS 20 (1985) were more reflective of Australian practice by reinstating the current rate method as an acceptable method. The current rate method should be used for self-sustaining operations and the temporal method for integrated operations. This decision, however, may have had more to do with harmonizing with FAS 52 and SSAP 20 than with reflecting current practice. When the current rate method is used, translation gains and losses are taken to reserve accounts. Under the temporal method, short-term gains and losses are taken to the income statement and long-term gains and losses are deferred and amortized over the life of the asset or liability. The reserve treatment coincided with the minority practice but again this choice may reflect a desire to harmonize with FAS 52 and SSAP 20. Income statement treatment for gains and losses was confined to short-term items when using the temporal method, which again does not reflect Australian company practice. ASRB 1012, issued in 1987, and an amended AAS 20 did away with the amortization option and required that long-term gains and losses be taken to the income statement, again, a step towards harmonizing with FAS 52 and SSAP 20.

Australian pronouncements on foreign currency accounting reflected, then deviated, then compromised with Australian company practice. The deviations are not fully explained and the compromises appear to have more to do with harmonization of standards by other countries. The choice of methods by the AARF in developing these standards appears to have less to do with current practice than some other factors.

The first Canadian pronouncement on foreign currency accounting, the 1977 ED

which endorsed the temporal method, clearly did not follow current Canadian practice. According to a survey by the CICA[32] no Canadian companies used the temporal method as a basis for translation in 1973 and 1974 and only 2 did so in 1975 and 4 did so in 1976. 40-50% of companies surveyed for the years 1973-76 used the current-noncurrent method and approximately 13-15% used the current rate method. The rest of the companies used other methods or the methods were indeterminable. More companies used the temporal method after the issuance of the 1977 ED, but the current-noncurrent and current rate methods continued to be the preferred methods from 1977 through 1982.[33] Though AR 1650 endorsed the current rate method for independent operations, the endorsement of the temporal method for integrated operations reflected the preferred methods of the US standards, not Canadian company practice.

Prior to the ED in 1977, the majority of Canadian companies preferred some type of deferral treatment for unrealized exchange gains and losses. In the years 1973-76, less than 20% included gains and losses immediately in the income statement.[34] The ED required the deferral treatment on long-term monetary assets and liabilities only, a treatment which was not used by any of the 325 companies surveyed prior to 1978. From 1978 to 1982, the deferral treatment of long-term monetary items was used by a greater number of companies. Less than 25% of the companies preferred immediate recognition

---

32
CICA, *Financial Reporting in Canada,* 12th edition, (Toronto: CICA, 1977), p. 18.

33
Ibid., 14th and 15th editions, 1981 and 1983, respectively.

34
Ibid., 12th edition.

of gains and losses.[35]

The treatment of long-term monetary gains and losses was a controversial topic because the Canadian pronouncements followed the US pronouncements closely except for this item. The US pronouncements required immediate recognition of these gains and losses and it was on this item that the Canadian pronouncements differed the most from the US standards. The deferral treatment was consistent with the general practice of deferral for gains and losses for Canadian companies, but the companies surveyed did not use this treatment for long-term monetary items until after the first pronouncement was issued. Another pertinent fact is that the 1977 ED was suspended in 1979 after controversies arose surrounding FAS 8. Companies continued to defer gains and losses on long-term monetary items from 1979-1982 in spite of the suspension. The deferral treatment on long-term monetary items was not in line with Canadian company practice and there is little evidence from company surveys to support the different treatments for independent and integrated operations that was ultimately endorsed by AR 1650. Overall, the Canadian pronouncements do not reflect the practice of Canadian companies for foreign currency accounting.

The discussion indicates that standard-setters did not follow current practice consistently in developing the specific provisions pertaining to translation method and the treatment of gains and losses. Overall, the standards prescribed treatments for gains and losses that differed substantially from current practice in these countries. To what

---

35

Ibid., 14th and 15th editions, 1981 and 1983, respectively.

extent current practice explained the method of translation varies among the standards. In the US, practice involved the use of several methods and combinations of methods and standards clearly did not reflect such diverse practice. In the UK, however, the standards did reflect the most widely used method of translation in the UK, but also permitted the temporal method which was endorsed in the US but not widely practised there prior to FAS 8. The situations were similar in Canada and Australia, where the endorsement of the current rate method reflected practice but the temporal method did not. The standards reflected the popularity of the current rate method but current practice does not explain the endorsement of the temporal method. Ultimately, the consensus that was reached among the standards in these countries endorsed both of these methods. The differences in the early standards on foreign currency and the subsequent movement towards harmonization had something to do with the translation methods most commonly used by MNCs but not entirely. The recommendations of the standard-setting bodies suggest some attempt to harmonize with other countries. However, the degree of consensus that was reached was based only in part on current practice for translation method and had less do to with current practice for treatment of gains and losses.

II. Accounting Principles Argument

One of the criticisms of the current-noncurrent, monetary-nonmonetary, and temporal methods of foreign currency translation concerns the lack of conceptual justification for the balance sheet classifications in determining which exchange rate to

use.[36] The current-noncurrent and monetary-nonmonetary methods were also criticized for not reflecting economic reality.[37] Surveys of practice indicate that the current-noncurrent method was still widely used in the early 1970's,[38] in spite of the sentiment that the method did not reflect the current business environment.[39] If current practice was not the only factor in choosing methods for foreign currency accounting, another view might suggest that choices were based on a conceptual framework or certain accounting principles. In the case of the US, the FASB did not issue a Discussion Memorandum on the development of a conceptual framework until 1976[40]. That is not to say that early developments concerning a conceptual framework did not influence the development of FAS 8 (which was issued in 1975), but that a pronouncement on a conceptual framework did not exist prior to the development of FAS 8, and certainly not before the ED of 1974.

Nevertheless, the Board expressed certain accounting principles as the rationale for endorsing the temporal method FAS 8. According to the 1974 ED, the historical cost basis of accounting was cited as the main argument against endorsing the current rate

---

36 Willey, *ibid.*, 1977; Choi and Mueller, *ibid.*

37 Kubin, *ibid.*; Parker, *ibid.*; Harris, *ibid.*; Choi and Mueller, *ibid.*

38 Willey, *ibid.*, 1977.

39 Mueller, *ibid.*, 1965.

40 Donald E. Kieso and Jerry J. Weygandt, *Intermediate Accounting, Seventh Edition* (New York: John Wiley & Sons, Inc., 1992).

method and the current-noncurrent method.[41] The Board also expressed concerns over retaining the measurement bases of financial statement items[42] and how classification schemes of both the current-noncurrent and monetary-nonmonetary methods fail to maintain that objective.[43] The Board defended the endorsement of the temporal method on the grounds that it translates assets and liabilities carried at past, current, or future prices; thus, the measurement bases are retained for foreign statement items.[44]

The FASB later reconsidered and permitted the current rate method for independent operations and operations in highly inflationary economies in FAS 52. The rationale is supplied by the functional currency approach, which recognizes that independent foreign entities incur costs and receive revenue in the currency of their economic environment as well as maintaining the balance sheet in that currency. Using the current rate retains "in the consolidated financial statements the inherent relationships appearing in the functional currency financial statements".[45] So while considerations over accounting principles were perhaps the basis in developing FAS 8, it

---

41 FASB, *Exposure Draft: Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements* (Stamford, CT: Financial Accounting Standards Board, December 31, 1974) paras. 82 and 87.

42 *Ibid.*, para. 51.

43 *Ibid.*, paras. 89 and 93.

44 *Ibid.*, para. 97.

45 FASB, *Statement of Financial Accounting Standards No. 52: Foreign Currency Translation* (Stamford, CT: FASB, December 1981), para. 98.

appears that these considerations did not carry through in the later pronouncement. In the case of FAS 8, the rationale of accounting principles could also have been used to justify ex post the choice of methods made on some other basis.

The Board again held firm on the principle of retaining the measurement basis of assets and liabilities in deliberating over the treatment of translation gains and losses. In arguing against amortizing gains and losses over the life of assets held at historical cost, the Board rejected the "cover" approach. In the cover approach, when a net liability position exists,

> the dollar equivalent of an exposed net liability position is offset (deferred) against a potential change in the future dollar value of assets carried at cost...However, the Board believes that offsetting is not proper under present generally accepted accounting principles that recognize certain gains and losses when values change and others only at time of sale or other disposition. If offsetting is desirable at all, it should be accomplished by changing general accepted accounting principles to recognize changes in the dollar value of *both* items. However, to do so would require reconsideration of historical cost as a fundamental concept of accounting,[46]

which the Board stated was beyond the scope of the statement.

In arguing against amortizing gains and losses over the life of long-term liabilities, the Board took the position that "an exchange gain or loss resulting from the adjustment of accounts denominated in foreign currency should be immediately included in the determination of net income so as to properly report the results of that situation at

---

[46] *Ibid.*, para. 119.

the time it occurs."[47] The Board also rejected the adjustment of stockholders' equity for translation gains and losses on the basis that these gains and losses "should be included in the determination of net income in accordance with the all-inclusive income statement presently required by generally accepted accounting principles."[48]

Another proposal rejected by the Board concerned the deferral of unrealized gains and losses while realized gains and losses would be recognized immediately in the income statement. The Board saw no theoretical justification for distinguishing between realized and unrealized gains and losses and that this distinction would be difficult to implement.[49] A related view based on the concept of conservatism would defer only unrealized exchange gains, but the Board viewed that proposed method as an inconsistency in the translation process. "Although the concept of conservatism may be appropriate in other areas of accounting, the Board believes its application to translation of financial statements is inappropriate...To defer an exchange gain solely because it is a

---

47 *Ibid.*, para. 77.

48 *Ibid.*, para. 122. APB Opinion 9 recommends that any gain or loss experienced by the concern, whether directly or indirectly related to operations, should be included in the income statement because it contributes to the long-run profitability of the company and that any judgment concerning the handling of gains and losses may result in the manipulating of income (Kieso and Weygandt, 1992). In FAS 8 (para. 198-199), the Board further argued against the implication that a function of accounting is to minimize the reporting of fluctuations: "Exchange rates fluctuate; accounting should not give the impression that rates are stable."

49 *Ibid.*, para. 124 and 126.

gain would in effect deny that a rate change has occurred."[50] In this case, the accounting principle of conservatism was rejected as a basis for endorsing a method of accounting for gains and losses.

What is ironic is that on the one hand, the Board rejected conservatism in the handling of gains and losses but that the lack of conservatism was cited as the reason for the rejection for the current-noncurrent method.[51] Here conservatism is a reason for the "unpopularity" of the current-noncurrent method but was not a reason for deferring unrealized gains. In the case of gains and losses, the Board took the least conservative viewpoint by requiring that the gains and losses be run through the income statement. What is puzzling is the point of view that conservatism is appropriate in other areas of accounting but not for foreign currency accounting. The pronouncements are not clear on why this is so. The FASB expressed some accounting principles, such as historical cost and measurement issues, as the basis for developing the standards for foreign currency accounting but were not consistent in their application of certain concepts, such as conservatism. Nor did the Board adhere to these reasons for rejecting proposals for the use of the current rate method for independent operations and operations in inflationary economies. An argument that accounting principles guided the choice of methods for foreign currency accounting can be shown to be only partially correct and does not fully explain the endorsements by the FASB.

---

50 *Ibid.*, para. 127-128.

51 FASB, *ibid.*, 1975, para. 125.

The UK EDs made fewer references to accounting principles in developing SSAP 20 than did the US EDs in developing FAS 8 and FAS 52. SSAP 20 refered to the UK concept of a "true and fair view" and the concept of accrual accounting in discussing the rationale for reporting exchange gains and losses on the income statement.[52] The concept of recognizing gains and losses in the period in which they occur (similar to the all-inclusive argument in the US) showed up in the rejection of spreading exchange differences over the life of loans.[53] However, as in FAS 8, the rejection of a conservative approach to reporting unrealized gains in favour of a symmetric treatment of gains and losses occurred in SSAP 20.[54] This symmetric treatment of gains and losses applied to both short-term and long-term monetary items. This distinction was an important feature of UK standards on foreign currency accounting because it departed from Schedule 8 of the UK Companies Act 1948 which specifies that only profits realised at the balance sheet date shall be included in a company's profit and loss account:

> Since the inclusion of unrealised exchange gains in the profit and loss account is a departure from an accounting principle set out in Paragraph 12 of Schedule 8, ASC considers it more appropriate to invoke Paragraph 15 of that Schedule which specifically permits a departure from the accounting principles where there are special reasons. In SSAP 20 the necessity to show a true and fair view of results, based on the need for symmetry explained ..... above, is considered to constitute a

---

52 Accounting Standards Committee, *ibid.*, 1983, para. 10.

53 Appendix 3, Basis for conclusions reached in the UK and Ireland, ED 27, *Accounting for Foreign Currency Translation*, para. 121.

54 *Ibid.*, para. 10.

special reason for departure from the principle under Paragraph 15 of the Schedule.[55]

So while certain accounting concepts (true and fair view, all-inclusive income) justified or rationalized the departure from current practice in the UK (in taking exchange gains and losses to reserves) certain other accounting concepts were not considered. The concept of historical cost accounting, for example, which was considered important in the development of US standards, was largely disregarded in the UK standards. The cover approach that was rejected in the US on the basis of historical cost was endorsed by the UK standards.

The endorsement of the current rate method also rejected the historical cost concept in favour of 'practical' concerns regarding retaining the financial relationships (i.e., financial ratios) that existed prior to translation: this "method of translation ensures that the translated results and relationships do not differ significantly from those reported prior to translation".[56]

As mentioned in the previous section, the temporal method was permitted to accommodate US subsidiaries in the UK and was justified in the standards as being useful for preparing consolidated financial statements in circumstances where the overseas operation is basically a sales agency for the holding company.[57] The premise

---

55

Appendix 2, Technical Release issued by the Accounting Standards Committee on the publication of SSAP 20, *TR 504,* April, 1983, para. 12.

56

Ibid., para. 7.

57

Appendix 3, Basis for conclusions reached in the UK and Ireland, ED 27, *Accounting for*

was based on the notion that more independent operations would secure local sources of finance and develop into a "business entity" with its own tangible assets.[58] But the temporal method was basically rejected as the principal method of translation in the UK because of the inconsistency in translating assets at historical rates while translating loans at current rates. Independent foreign operations were considered a "net investment" by UK standard-setters and thus different treatments for assets and liabilities did not make sense.

The choice of translation methods by the ASC in developing ED 21, ED 27, and SSAP 20 was generated in response to practical concerns about the implementation of FAS 8. The choice of treatment of exchange gains and losses, however, seemed to be based on concerns over a "true and fair view" and, though not specified as such in the pronouncements, an all-inclusive approach to reporting income, which in fact departs from the Companies Acts. As in the case in the US, the basis of accounting principles explain some of the provisions in the UK standards on foreign currency accounting, but not all.

The rationale for choice of methods in the Australian pronouncements on foreign currency accounting changed with each pronouncement. The current rate method was endorsed in 1973 and the choice was based on rather weak reasoning and, perhaps, a misconception of the current rate method's ability to retain historical cost:

Foreign Currency Translation, para. 116.

58

Appendix 2, Accounting for foreign currency translations--the options considered by the ASC, *Ibid.*, para. 80.

The current rate at the end of the period is the relevant one to the users of the financial statements of an Australian company, thereby justifying its use for this purpose. The basis of accounting (for example, historical cost) adopted in the foreign-currency statements remains unaffected, and the results and position of the operation, having been fairly reported (and audited), are then translated in a simple, convenient, and relevant manner.[59]

This statement reveals only the prevalence of current practice and was based more on convenience than any accounting principle.

The Australian ED in 1979 (ED 11) focused more on accounting principles in arguing the choice and rejection of the various methods of translation. The current-noncurrent method was rejected because of the effect of its classification scheme on the treatment of inventory.[60] The rejection of the monetary-nonmonetary method also reflected a concern over the translation of items that had been revalued and the difficulties with retaining the measurement basis:

This distinction between monetary and non-monetary is not seen to be an appropriate basis for the application of a different exchange rate. Translating non-monetary items at historic (past) exchange rates produces reasonable results if the items are stated at historical (past) costs but not if they are stated at current prices.[61]

Similarly, the current rate method was rejected because of valuation concerns:

...the translation method will involve a departure from the 'lower of cost and net realisable value' principle. This method of translation will also produce

---

59

Australian Society of Accountants and the Institute of Chartered Accountants in Australia, ED 4, *Proposed Statement of Accounting Standards: "Translation of Amounts in Foreign Currencies"* (September 1973) para. 13.

60

Australian Accounting Research Foundation, ED 11, *ibid.*, 1979, Appendix 1.

61

Ibid.

significant unrealised exchange gains and losses when translating fixed assets. The inclusion in the results for a period of material exchange gains and losses in respect of fixed assets will lead to the presentation of financial statements which lack commercial realism.[62]

The convenience of the current rate method was not enough to offset the concerns over valuation principles. The temporal method was endorsed primarily on this principle, i.e., that it retains the basis of valuation.

The 1983 ED (ED 24) and subsequent pronouncements showed a change of heart regarding the current rate method. By this time, FAS 52, with its functional currency approach, and SSAP 20, with its self-sustaining versus integrated classification for foreign operations, were in effect. They both advocated the current rate method for independent operations and the temporal method for those operations considered an extension of the parent company. ED 24 adopted the current rate method with the reasoning that this method would preserve the results and financial position of a self-sustaining operation (para. 16) while the temporal method would do so for foreign operations closely linked to the parent company by incorporating the activities of the foreign operation as they had been entered into by the parent company (paras. 19, 20, and 21). The main concern seems to be preserving a measure of valuation that retained the results of operation and financial position in the translation but it did not seem clear which method would accomplish this objective. The inconsistency over choice of method reflects something other than accounting principles and more likely the Australian attempt to harmonize with the pronouncements of other countries.

---

62 *Ibid.*

The Australian pronouncements show a similar inconsistency regarding the treatment of translation gains and losses. In ED 4 (1973) deferring gains and losses over some time period was rejected: "There is no logical accounting basis, such as matching costs with revenue, for deferring recognition and spreading gains and losses over future accounting periods."[63] Recognizing losses and deferring gains, though recognized as conservative, was rejected for inconsistency. Reserve accounting for these gains and losses was rejected on the grounds that it is "not considered acceptable practice", which reflects the majority of companies that were surveyed, even though one-third of the companies did indeed take these gains and losses to a reserve account. The preferred method was the recognition of both gains and losses immediately in the income statement on the basis that it is the only method providing "adequate accounting and disclosure".[64] Again, this treatment of gains and losses reflected the majority of current practice, with little or no basis on accounting principles.

In ED 11 (1979) an accounting concept was offered for the rejection of reserve accounting. Recognizing gains and losses through reserve accounts: "...represents a departure from the concept of an all-inclusive profit and loss statement as embodied in existing accounting requirements."[65] The recognition of gains and losses in the income

---

[63] Australian Society of Accountants and the Institute of Chartered Accountants in Australia, ED 4, *ibid.*, para. 18.

[64] Australian Accounting Research Foundation, ED 11, *ibid.*, Appendix I.

[65] *Ibid.*, para. 13.

statement was still considered appropriate for short-term receivables and payables but could cause undue fluctuations in the results from period to period if applied to long-term receivables and payables. Thus, the method of deferring the gains and losses to deferred income and expense accounts was defended on the grounds that it:

> ...results in a more appropriate matching of the costs of borrowing with the benefit derived from the use of funds borrowed .....requires exchange gains and losses to be included in the profit and loss statement over the period to settlement and has the advantage of being prudent.[66]

From previously having no logical accounting basis for this treatment, the matching of costs and benefits was deemed by the Australians as an important reason for implementing the deferral treatment.

When ED 24 (1983) adopted the current rate method, reserve accounting was adopted as an acceptable approach. The concerns for practice in ED 4, and for the theory of all-inclusive income in ED 11, were set aside to accommodate the current rate method.[67] When using the temporal method, the profit and loss treatment for short-term gains and losses was required. Long-term gains and losses under the temporal method required the deferral method for reasons similar to those stated in ED 11.[68] ED 24 (1983) and AAS 20 (1985) endorsed the deferral approach for long-term monetary items which differed from the income statement treatment of FAS 52 and SSAP 20. The Australian

---

[66] *Ibid.*, para. 16.

[67] *Ibid.*, para. 18.

[68] *Ibid.*, paras. 10 and 11.

standard-setters conformed to FAS 52 and SSAP 20 in the classification of independent and integrated foreign operations and their respective treatments except for the treatment of gains an losses on long-term monetary items in 1985. That method was later rescinded in ASRB 1012 and the amended AAS 20 in 1987 which required that these gains and losses be run through the income statement.

The Australian pronouncements are fraught with contradictions in the choice of methods. This is true in the rejection of the current rate method in ED 11, in its reinstatement in ED 24, and in the rejection of both reserve and deferral methods of treating gains and losses. Although concepts of valuation and all-inclusive income served as the basis for some of the arguments in ED 11, these concepts were excluded in ED 24. Matching as a basis for treating gains and losses was rejected in ED 11 but later served as the basis for instating the deferral method in ED 11 and ED 24. Although such evidence suggests the (ad hoc) use of accounting principles as a basis for these standards, the ambiguity concerning these concepts provides very little evidence to support the notion that the use accounting principles by standard-setters was responsible for the outcomes of the standards.

The Canadian pronouncements recommended methods very similar to the US pronouncements. The historical principle was used to justify the choice of the temporal method in the 1977 ED: "The temporal method translates assets and liabilities carried at past and current prices in a manner that retains their valuation bases and at the same time

uses the Canadian dollar as the unit of measurement,...."[69] However, the temporal method did permit current valuation of assets and liabilities. Interestingly, in the later pronouncements, the CICA did not justify the choice of methods. The 1982 ED and AR 1650 only specify the rules to be followed. No reason is offered to explain the classification scheme for integrated and independent operations.[70]

A major difference between the US and Canadian standards was, however, the treatment of gains and losses on long-term monetary items. The first draft of the ED, issued in May 1977, endorsed the amortization of the gains and losses over the total life of the asset or liability. The justification for this treatment was given as follows:

> when borrowing or lending funds in a foreign as opposed to domestic currency, an enterprise incurs an additional risk which will materialize if the exchange rate differs at the date of repayment. The cost or income associated with this risk may be considered as an element of the total cost or gain of borrowing or lending foreign currency funds and accordingly relates to the period of time during which the funds are outstanding.[71]

In this sense, the gains and losses were considered as an element of the total cost of borrowing or lending but it was not clear why this method was preferred over any other treatment. In a subsequent draft of this ED, issued in 1978, the amortization period was changed to the remaining life of the asset or liability, in response to comments by

---

69 CICA, Exposure Draft, *ibid.*, 1977, para. .22.

70 Stephen Spector, "Standards Update", *CGA Magazine* (August 1982): 5.

71 Moore, *ibid.*, 1977.

respondents.[72] This treatment was not based on any accounting concept and it has been suggested that it was adopted for the purpose of reducing fluctuations to net income which was a weakness of the immediate recognition treatment of FAS 8.[73] AR 1650 retained this treatment of gains and losses on long-term monetary items without further discussion.

There appears to be very little justification for the choices made by the CICA in developing standards for foreign currency accounting based on accounting principles. On those provisions that were similar to the current US pronouncements, the CICA made corresponding arguments for the historical principle. However, many of the choices in the later Canadian pronouncements were made without any justification whatsoever. Because of the correspondence between AR 1650 and FAS 52 and SSAP 20, one might argue that choices were made by the CICA in the spirit of international harmonization. However, a desire for harmonization does not explain the difference in treatment for gains and losses on long-term monetary items. For this item, the rationale appears more likely as a response to reduce fluctuations in net income with "no support from a theoretical point of view".[74]

The IASC also issued pronouncements on foreign currency accounting. The choice of methods has been consistent, permitting both the current rate method and the

---

[72] David J. Moore, "Foreign currency translation", *CA Magazine* (September 1978): 76-80.

[73] Willey, *ibid.*, 1979.

[74] *Ibid.*

temporal method in specific circumstances. These choices have been made primarily on practical grounds of accommodating more than one view point. "Under these circumstances it is not possible to select only one of the two methods as the international standard and to expect universal acceptance. The Standard accepts either of these two methods."[75] The type of operation determines the translation method, according to the IASC. From the first pronouncement, E 11, issued in 1977, the temporal method was endorsed for foreign-based operations viewed as extensions of the parent company. The current rate method was endorsed for those foreign-based operations viewed as separate business units in which financial statements prepared in the foreign currency were considered the most meaningful.[76] Standards up to that point in time in the US, Australia, and Canada had chosen one method or another. Only the UK had permitted both. E 23 and IAS 21 endorsed both methods but emphasized the necessity to evaluate the relationship between the foreign operation and the parent company in choosing a translation method so as to preserve the results of operation and financial relationships for meaningful indicators of performance for each type of operation (i.e., independent versus integrated).[77]

Treatment of gains and losses on translation was similar to the Canadian

---

75

IASC, Exposure Draft 11, *Accounting for Foreign Transactions and Translation of Foreign Financial Statements* (London: IASC, 1977), para. 17.

76

Ibid., paras. 13 and 15.

77

IASC, Exposure Draft 23, *Accounting for the Effects of Changes in Foreign Exchange Rates* (London: IASC 1982), paras. 18-19.

treatment under the temporal method. In E 11, gains and losses were to be run through the income statement (immediate recognition) under the temporal method except for those pertaining to long-term monetary items, which could be either deferred and amortized or taken to reserves. Under the current rate method, income statement treatment was recommended except for those items with uncertainty regarding realization. These were also deferred or taken to reserves. The US, UK, and Australia had recommended immediate recognition in the early pronouncements at the time that E 11 was issued. In E 23, only reserve treatment was permitted for the current rate method, which coincided with the standards from the other countries. However, there was virtually no explanation of these choices by the IASC. The choices made seemed to reflect very little concern for accounting principles.

Results of analysing accounting principles as the basis for choices made by standard-setting bodies for foreign currency accounting are mixed. Historical cost appeared to be the basis for endorsing the temporal method but later, when both the current rate and temporal methods were endorsed, the historical cost argument was replaced by a concern for retaining the value of ratios and other measurement issues in selecting a translation method. Issues of conservatism were inconsistently applied throughout. The all-inclusive income concept was applied as rationale for income statement treatment of gains and losses but only in the US and the UK. Canada and, for a time, Australia would endorse only deferral for gains and losses on long-term monetary items, but without an explanation based on accounting principles. Standards issued by the IASC gave little indication of regard for accounting principles and appeared to be

focused mainly on acceptance by the majority.

The consensus that was reached over the use of both the current rate and temporal methods can be attributed to something other than accounting principles. The standards would indicate inconsistency in the use of accounting principles in endorsing both methods, even under different circumstances, because they are diametrically opposed on the historical cost principle. The movement towards consensus on treatment of gains and losses appears to be motivated more by concerns over harmonization than any application of accounting principles. Consistent use of accounting principles seems to be overshadowed by other concerns. Ironically, the reconsideration and, to some extent, rejection of certain accounting principles allowed for a degree of consensus to be achieved among these standard-setting groups. Consideration for accounting principles was part of the deliberations in developing these standards, but in view of the inconsistencies, an argument for understanding choices made by standard-setting bodies based on accounting principles would be ambiguous at best.

III. Lobbying Efforts

The lobbying research on standard-setting for foreign currency accounting is similar to the pluralist view taken by Watts and Zimmerman in their study on the standard-setting process for general price-level accounting.[78] In that study, the authors

---

[78] R. L. Watts and J. Zimmerman, "Towards a Positive Theory of the Determination of Accounting Standards", *Accounting Review* 53 (January 1978):112-134.

construct a model that predicts which firms lobby on general price-level accounting. In that analysis interests are merely determined by membership in a social group (i.e., management) and are based on the size of their firm. Also, as Robson[79] points out, the managers' positions are assumed to explain their interests and at the same time the interests are revealed by the managers' lobbying actions. "...interests inform decisions which then determine actions, the latter in this case being lobbying behaviour. The demonstration of interests, however, depends upon the lobbying behaviour,..."[80] Furthermore, interests are identified only through outcomes and they ignore the possibilities that entities might mistakenly calculate their interests or that outcomes may be unintentional or the result of multiple rationales. Finally, interests that are imputed are not based only on individuals' own concepts of interests but also the interests expressed by others who may be in alliance with or offering resistance to the specific actors in question.[81] In other words, the interests expressed by a set of managers are not only their interests but may entail the interests of other groups or ideologies as well.

Concerning the examination of lobbying efforts, it should be noted that only the most visible forms of lobbying actions are taken into account, i.e., comment letters on exposure drafts of proposed standards. Lobbying efforts entail other forms of communication to the standard-setting bodies. For example, one corporation participated

---

79 Robson, *ibid.*, 1993.

80 *Ibid.*

81 *Ibid.*

on the foreign currency task force in its domicile, corresponded with members of the standard-setting body and its staff members, made numerous personal contacts and discussions, wrote articles published in accounting and other journals, and gave oral presentations at public hearings on the subject of foreign currency accounting.[82] Many of these types of lobbying activities are difficult to identify because of lack of documentation. Comment letters are the most visible and are well-documented. Many articles have been written on the subject of foreign currency accounting, most advocating one method or another.[83] These articles might also be considered a form of lobbying but it is not feasible to determine whether or not the members of the standard-setting bodies had read them all. It is assumed that comment letters were read and studied by the relevant staff and committee members in each standard-setting body.

Studies which take the pluralist approach in studying the standard-setting process

---

82

Stanley R. Wojciechowski, "DuPont Evaluates FAS 52", *Management Accounting* (July 1982): 30-35.

83

A sample of such articles include the following: Marvin M. Deupree, "Translating Foreign Currency Financial Statements to U. S. Dollars", *Financial Executive* (October 1972): 48-68; Alan F. Smith, "Temporal Method: Temporary Mode?", *Management Accounting* 59 (February 1978): 21-26; Russell W. Willey, "In Defense of FAS No. 8," *Management Accounting* 61 (December 1979): 36-40; D. R. Rickard, "Currency Translation", *The Australian Accountant* 50 (January/February): 10-11; Bradley M. Roof, "FASB No. 8--Did it Help or Hinder Multinational Reporting?", *Financial Executive* 50 (March 1982): 27-36; Peter H. Eddey and Frank W. Johnson, "Exchange Rates, Foreign Borrowings and Profit Distortion", *The Chartered Accountant in Australia* 53 (October 1982): 22-25; Rodney Jansz, "Foreign Currency Translation--The Continuing Debate", *The Chartered Accountant in Australia* 55 (July 1984): 40-41. The authors include professional accountants, academic professors of accounting, and corporate controllers. Many other articles were written in Canada and the UK as well as the US and Australia and some of them are referred to in other parts of this dissertation.

for foreign currency accounting include Kelly's[84] examination of the extent to which firms' debt contracts and managements' degree of ownership were associated with managers' decision to lobby the FASB in the form of comment letters on the proposed FAS 8. The study did not focus on whether the firms in the sample lobbied for or against the standard; rather, it focused on the decision to lobby itself. The results show that there was no significant difference in size or percentage of foreign sales between firms that lobbied and those that did not. A later study involving FAS 52 found that there was an inverse relationship between the decision to lobby and net income from foreign operations.[85] Kelly's results show that the management ownership proportion was lower in firms that lobbied on FAS 8 than those that did not, which was contrary to expectations. This result was supported in a similar test involving FAS 52.[86]

An earlier study[87] did examine the association of certain firm characteristics with opposition to the standard. Other studies also investigated characteristics of firms

---

84

Kelly, *ibid.*, 1985.

85

Robert J. Kirsch, Thomas G. Evans, and Timothy S. Doupnik, " FASB Statement 52, An Accounting Policy Intervention: U. S.-Based Multinational Corporate Preenactment Lobbying Behavior", *Advances in International Accounting* 3 (1990): 155-171.

86

Ibid.

87

Lauren Kelly, "Corporate Lobbying and Changes in Financing or Operating Activities in Reaction to FAS No. 8", *Journal of Accounting And Public Policy*, (Winter 1982): 153-73.

lobbying against FAS 8 and FAS 52.[88] The purpose of these studies was to provide a basis for predicting the consequences of proposed accounting policy change on firms to assist the FASB in assessing potential opposition to a standard. In all cases, predictive ability was rather limited as variables (firm characteristics) were only weakly associated with firms' positions on standards. In Kelly, lobbying activities were found to be unassociated with changes in financing or operating activities after adoption of FAS 8. Griffin (1982) found only limited support for the hypothesis that firms lobbying against FAS 8 reported wider fluctuations in pretax earnings than firms that did not lobby. In that study, the amount of foreign exchange gain or loss was not a significant characteristic of lobbying firms but in the later study (1983) in which he attempted to predict lobbying behaviour of firms on FAS 52 it was found to be significant.

A more relevant question for this study is, to what extent do firms' lobbying efforts affect the choice of accounting methods in the standard-setting process? Did firms' positions on translation methods affect the choices made by standard-setting bodies? Did firms' influence on the choice of accounting method vary among countries? In a critique of Watts and Zimmerman's positive theory concerning managerial self-interest which determines what standards managers will lobby for, Bryant[89] investigated

---

88

P. A. Griffin, "Foreign Exchange Gains and Losses: Impact on Reported Earnings", *Abacus*, 18 (June 1982): 50-69, and "Managements' Preferences for FASB Statement No. 52: Predictive Ability Results", *Abacus* 19 (1983): 130-138.

89

Bryant, *ibid.*

the relationship between the positions of lobbyists concerning FAS 8 and the final standard (FAS 52). A content analysis of letters submitted in response to a FASB invitation to comment on all current standards in effect at the time revealed that the greatest concern by corporate managers about FAS 8 was the treatment of exchange gains and losses (91% against the income statement treatment). Respondents did suggest improvements to FAS 8; however, none of them directly recommended the approach followed in FAS 52 for independent operations. The results support the contention that lobbying efforts are at best loosely coupled with the ultimate standards.[90] This section builds on Bryant (1988) by investigating the possible effects of lobbying efforts on the choices made by standard-setting bodies in the UK, Australia, and Canada.

An analysis of the 122 comment letters received by the ASC after the issuance of ED 21 shows that 39% were generally against the ED, 27% were in favour, and 34% favoured some provisions and were against others. Respondents included companies (49), professional accounting firms (23), representative bodies of accountants (25), other representative bodies (8), and individuals (17). The commentators by and large supported the use of two translation methods. The majority (70%) of commentators either did not state a preference for a method or accepted both the temporal method and the current rate method.[91] 19 out of the 49 (39%) companies preferred the current rate method only, which is a higher percentage than any of the other groups, but this

---

90

Solomons, *ibid.*

91

From Appendix 4 attached to discussion papers for ASC meeting held on May 30, 1979.

percentage does not reflect practice which, as indicated earlier, suggests that the current rate method was used by 90% of the companies surveyed. Commentator groups besides companies were evenly divided on treating gains and losses through reserves or some type of deferral and through the income statement. Companies preferred reserve treatment over income statement treatment (20 out of 29 companies that commented--69%) which reflects practice prior to 1975.

According to these statistics, the majority of those companies that chose to comment on ED 21 accepted two methods. Several comment letters emphasized a need to reduce the diversity of acceptable methods but these are in the minority. Rather than permitting two acceptable methods, the ASC decided to endorse the current rate method as the primary translation method for UK and Irish companies in ED 27 and SSAP 20 and recommended the temporal method only in cases where the subsidiary is a direct extension of the parent company. Commentators on ED 27 continued to question the use of the temporal method but they are in the minority. Many of those letters did not comment on translation methods.

Except for exchange gains and losses on fixed assets which go to reserves, the UK pronouncements mainly recommended income statement treatment for gains and losses. The income statement treatment was not preferred by the majority of companies responding to ED 21 but commentators were generally in favour of the provisions of ED 27. This may be a result of the cover concept which allows offsetting of gains and losses on assets and liabilities. Most of the comments on ED 27 concerned this provision, mainly because they felt that the requirement that the loan be denominated in the same

currency as the investment asset was too restrictive. Overall, ED 27 was found to be more favourable than ED 21 (88 commentators out of 107 in favour). The main difference between ED 27 and SSAP 20 were the new provisions concerning realised gains and losses that arose as a result of the changes in the Companies Act of 1981 (mentioned previously). Commentators did suggest in letters concerning ED 27 that the proposed changes to the Companies Act be considered in drafting SSAP 20.

Overall, commentators to UK standards were divided on the use of translation methods. Some were emphatically opposed to the temporal method and endorsed only the current rate method while the majority did not express a preference. The standards reflect the tolerance for these two methods, with a preference for the current rate method. The treatment of gains and losses, however, does not reflect the majority of lobbyists views. Reserve accounting was still endorsed by many commentators in the letters concerning ED 27; however, the cover concept may have been a solution to that problem. The cover concept was first discussed by the ASSC in April 1975 when the Committee requested that a paper on the topic be written by two individuals (named Watts and Ogle).[92] The Committee's first pronouncement, ED 16, was not issued until September 1975. Therefore, the first comment letters were received some time after the cover concept was initially considered by the Committee.

In Australia, submission letters on the 1973 ED largely reflected current practice. The preferred method by all but 2 out of 28 responses was the current rate method and 15

92
ASSC minutes of meetings, April 30, 1975.

out of 21 responses favoured the income statement treatment of gains and losses. The other 6 advocated the use of reserves.[93] 70 individuals or entities responded to the 1979 ED. Of the 40 that expressed a preferred translation method, 30 chose the current rate method. (The other 10 expressed a preference for the temporal method). Advocates of the current rate method were evenly divided on taking translation adjustments directly to reserve accounts and the income statement treatment. The income statement treatment for short-term gains and losses on transactions was almost unanimously supported by the respondents in 1979. For long-term monetary items 17 out of 42 preferred deferral and amortization of gains and losses and 15 out of the 42 preferred immediate recognition in the income statement treatment. 11 companies preferred deferral and only 6 companies preferred immediate recognition.[94]

There was more support for reserve treatment under the current rate method in the 1979 submissions than that in 1973 but the number advocating reserve treatment was roughly equal to those still advocating the income statement treatment. Similarly, respondents were almost evenly divided between deferral treatment and immediate recognition for gains and losses on long-term monetary items, a choice that is required under the temporal method. The 1983 ED reflects some of these preferences. Deferral was chosen for the long-term monetary gains and losses under the temporal method and reserve treatment for the current rate method gains and losses. Given that there was

---

93

Summary of submission letters on 1973 ED from AARF files.

94

Report on responses to foreign currency ED, June 1979, from the AARF files.

almost equal support for the alternative treatment, it cannot be said that the methods chosen were based on majority views of the submission letters.

AAS 20, issued in 1985, adopted the same methods as the 1983 ED. In December, 1986, the ASRB released Release 411 which raised questions concerning the deferral treatment on long-term monetary items. Although "a clear majority" of respondents to 411[95] favoured the deferral treatment, the ASRB in April 1987 requested the AARF in Media Release 87/1 to resubmit the standard on foreign currency accounting with a provision for immediate recognition of gains and losses on long-term monetary items. AAS 20 was amended by the AARF and re-issued in December 1987 which prescribed the immediate recognition. Clearly the revised standard did not reflect the preferences of the respondents in the submission letters to Release 411.

Responses to the 1977 Canadian ED came from 40 industrial companies, 15 individuals from such companies, 11 public accounting firms, 28 other individuals, 5 accounting organizations from Canada and other countries, and 1 from a provincial institute committee. On method of translation, there was no overwhelming support for any particular method. 10 favoured the temporal method, while 11 favoured the current rate method, 3 favoured the current rate method for self-sustaining operations, and 4 supported the current-noncurrent method.[96] Clearly the choice of the temporal method

---

[95] From "A Preliminary Review of Responses" to Release 411, March 1987, from the AARF files.

[96] Moore, *ibid.*, 1978.

by standard setters in Canada did not reflect the opinions of respondents who did not agree on what might be considered the best method. The majority of respondents to the 1982 ED, however, agreed with the situational approach (i.e., the temporal method for integrated operations and the current rate method for self-sustaining operations).[97] Only 3 respondents to the 1977 ED suggested the current rate method for self-sustaining operations. Some respondents to the 1982 ED expressed difficulty with this approach from a conceptual standpoint but supported it in the interest of international harmonization,[98] perhaps the dominant factor in the Canadian case. Canada's heavy dependence on foreign markets[99] may explain the Canadian interest in harmonization in order to facilitate transactions in foreign markets.

As for the treatment of gains and losses on long-term monetary items, again, there was no clear consensus among respondents to the 1977 ED. Six respondents agreed with amortization over the total life of assets and liabilities, while 15 endorsed amortization over the remaining life of the item, and 10 favoured the immediate recognition treatment of FAS 8.[100] As noted earlier, the CICA changed the earlier draft to coincide with those respondents that favoured amortization over the remaining life. But respondents to the

---

97 Jonathan M. Kligman, "Foreign currency translation: from exposure draft to standard", *CA Magazine* (June 1983): 57-60, 62.

98 *Ibid.*

99 McCallum, *ibid.*

100 Moore, *ibid.*, 1978.

1982 ED, which endorsed the same treatment were evenly divided between deferral and immediate recognition. The CICA, however, chose to retain the deferral method on the basis of "the arguments in support of the exposure draft...were more convincing than those in support of the other positions."[101] While at first it appeared that the CICA were following the majority opinion on gains and losses, there really was no majority opinion when the final standard was issued. Like the other countries in this study, the Canadian case does not provide support that lobbying efforts as measured by a count of comment letters to EDs were the key factor in the choices made by standard-setters.

Responses to the IASC's first ED, E 11, came from 16 countries. Twelve countries had general comments. Two countries (Rhodesia and Sri Lanka) expressed no comment. Of the remaining 10, 6 (Canada, Denmark, the Netherlands, Norway, South Africa, the UK) opposed the number of options available and commented that too many methods did not benefit harmonization and were against the provisions of E 11. One country (New Zealand) supported it without qualification, another supported it but thought that gains should be deferred (Argentina). Another supported it but recommended deferring unrealized gains and losses (the US). One country commented only on terminology (Australia). The majority believed that there was too much flexibility in the ED.

The IASC eliminated the immediate recognition and deferral options under the current rate method in E 23. General responses to E 23 came from 10 countries. Support

---

101
Kligman, *ibid.*

with some qualification was expressed by 6 countries (Australia, the Netherlands, Switzerland, the United Arab Emirates, the UK, and Canada). Switzerland favoured immediate recognition for all gains and losses. The UK expressed a desire that the ED conform to UK pronouncements but thought that the new ED more closely conformed than E 11 did. Canada expressed a desire for conformance with FAS 52. Two countries (New Zealand and the US) expressed concern over the number of options, with the US recognizing the need to accommodate many countries but still preferring the temporal method. One country (Sweden) preferred the temporal method also, with immediate recognition of gains and losses, so was in dissent as far as E 23 was concerned. Finally, Denmark was concerned about relating the net investment method to specific assets and had reservations concerning the deferral of gains and losses on long-term monetary items. Whatever these comments expressed, the IASC did little to change IAS 21 from the ED. The provisions concerning translation method and treatment of gains and losses are virtually the same as in E 23.

The evidence provides some support for the influence of lobbying efforts through submission letters to the standard-setting bodies on the outcomes of standards. However, the evidence is rather mixed. In the UK, standards overall reflected the tolerance for two translation methods by respondents but treatment of gains and losses did not always coincide with the majority view. Similarly in Australia, the treatment of gains and losses endorsed in the standards differed from respondents' majority view. In Canada, with little majority opinion on any method or treatment, the standards are based on some factor other than lobbying efforts through comment letters. Although lobbying efforts

through comment or submission letters cannot be ruled out as an influential factor in the different choices made by standard-setting bodies in these countries, there is not enough favourable evidence to suggest that differences can be attributed to lobbying efforts. Also, the eventual consensus that was reached cannot be fully attributed to comment letters. Provisions such as the cover concept and the use of translation methods in particular circumstances have very little correlation with the comments made in these letters. Clearly, there were other factors influencing the choices that resulted in the current standards.

IV. Tax Considerations

Tax laws could influence the choices for translation method and treatment for gains and losses in these countries. So far in this study, the choice of translation methods may be attributed in a limited way to current practice or concerns over accounting principle and perhaps currency devaluations and lobbying efforts. The main differences to be resolved to achieve harmonization were the treatments of gains and losses. The tax effects of gains and losses on foreign currency could influence the choices made by standard-setting bodies, depending on the tax laws in each country and any participation by tax authorities (and companies) in the process. Tax effects could have significant cash flow consequences for companies and for tax revenue for countries. This section investigates the possible association of tax laws with accounting standards in the US , the UK, Australia, and Canada. The evidence suggests little support for such an association.

The main concern of tax authorities is the tax treatment of profits to the parent company from the foreign subsidiary because generally it is only when a company reports a profit that a tax liability is incurred. Therefore, the tax rules focus on the translation of the income statement and foreign currency transactions. The translation of the balance sheet and the resulting gains and losses are less controversial for tax purposes than the translation of the income statement.

In the US case, unrealized gains are not taxable and unrealized losses are not deductible, according to a 1976 UK survey[102] of tax treatments for foreign currency gains and losses. FAS 8, which was issued in the previous year, required unrealized gains and losses to be included in the income statement; but companies could not claim unrealized gains and could not deduct unrealized losses for tax purposes. Another issue concerned the nature of realized gains and losses as to whether they are related to capital transactions (and would be taxed at the lower capital gains rate) or to revenue (in which case they would be taxed at the ordinary rate). The most controversial aspect is that of realized gains and losses on loan transactions. In 1976 when the survey was conducted, FAS 8 was already issued but there was considerable uncertainty as to whether gains and losses on loan transactions should be taxed or deducted at ordinary rates or capital gains rates. At the time that FAS 52 was issued, case law on the subject was still ambiguous on this topic.[103]

---

102 The Consultative Committee of Accountancy Bodies, TR 209, *ibid.*, 1976.

103 Andre M. Saltoun, "Tax Aspects of International Exchange Transactions", *Proceedings*

In the US at the time of the development of FAS 8, the tax laws permitted five methods of accounting for the tax effects of foreign currency transactions. Under the specific transactions method, foreign transactions are translated at the exchange rate on the day of the transaction. Taxable income includes the gain or loss on the transaction plus any exchange gain or loss affecting the foreign assets and liabilities. This method is governed by two principles: the separate transaction principle and the closed transaction principle. Under the separate transaction principle, gains and losses from the payments in foreign currency for goods and services are treated as separate from the purchase of the goods and services. This arises because payments are usually made later than the purchase, so the purchase is recorded at one exchange rate and the payment at another. Therefore, a gain or loss may occur when the payment is made. Gains and losses may also be incurred when funds in foreign currency are withdrawn before payment is actually made. Under the closed transaction principle, these gains and losses would not be recognized until the foreign funds have been converted into US dollars and the transaction is completed. FAS 8 accepts the separate transaction principle but rejects the closed transaction principle and permits the unrealized gain or loss on foreign funds to be recognized and recorded on the balance sheet date, whether or not they have been withdrawn or the transaction been completed.[104]

Three other methods permitted by the Internal Revenue Service in the US in the

---

from the 40th Annual N. Y. U. Institute on Federal Taxation (1982): Chapter 34.

[104] Michael L. Moore and John L. Kramer, "Tax and Accounting Rules for Currency Translation," *International Tax Journal* 3 (February 1977): 238-73.

late 1970s were not specifically endorsed by FAS 8. The first two methods are for branch operations. Briefly, under the profit and loss method, the branch profit that is remitted to the parent company is translated using the exchange rate on the day of the remittance. Under the net worth method, the translation is made from the balance sheet. The individual balance sheet items are translated at beginning and year-end using a method that corresponds to the current-noncurrent method. The change in net worth from this translation is the taxable income. The third method, called the foreign corporation method, is used for determining foreign tax credit on dividends from a foreign corporation that is not controlled. (Controlled foreign corporations must use a method called Subpart F, which is discussed below). Under the foreign corporation method, exchange gains and losses on foreign investments are not recognized for tax purposes until realized through remittances to the US. For financial reporting purposes, dividends payments require the specific transactions method.[105]

The fifth method, the Subpart F, pertains to US taxpayers owning 10 percent or more of a foreign corporation. The taxpayer must include its pro rata share of the foreign operation's income in the taxpayer's gross income. This includes operating profits and exchange gains and losses. The Subpart F method is similar to the net worth method in that it adjusts operating profit from the income statement for foreign exchange gains and losses pertaining to certain assets and liabilities used to arrive at operating profits. However, the method of translating assets and liabilities more closely resembles the

---

105
Ibid.

temporal method endorsed by FAS 8, with some exceptions.[106]

For the most part, the methods endorsed by the US tax laws differ significantly from the accounting rules for financial reporting purposes under FAS 8. As the example in Appendix IV indicates, the temporal method is disadvantageous for corporations when the dollar is falling because there is a loss on the books plus a tax liability. The dollar was falling during the 1970s, making the temporal method a potentially unlikely choice for accounting standards if tax effects were to be considered (unless, of course, the standard-setters were interested in raising tax revenue; there was no evidence to suggest that they were.)

The US tax requirements for foreign exchange gains and losses remained the same until 1986, long after FAS 52 was issued. The Treasury Department issued a discussion draft on the subject in 1980, *Taxing Foreign Exchange Gains and Losses.* It did not carry the force of law,[107] however, it did propose a change in the tax laws that corresponded with the functional currency approach in the FASB 1980 ED, which preceded FAS 52. This approach was also proposed in *The President's Tax Proposal to the Congress for Fairness, Growth, and Simplicity,* issued in May 1985, prior to the new tax law in 1986.

It might be argued that the tax laws then currently in force influenced the decision to endorse the current rate method because of the tax effects of the temporal method.

---

106 *Ibid.*

107 Saltoun, *ibid.*

There was little mention of tax effects in response letters to either FAS 8 or the ED leading up to FAS 52. The standards themselves offer little discussion of tax issues except for intraperiod tax allocation. Tax minimization is one of the rationales offered by Watts and Zimmerman[108] for lobbying the standard-setting process but for foreign currency accounting the tax issue was not raised by lobbyists.[109] Thus it is not clear that tax treatments for gains and losses on foreign currency accounting was a major issue in the US in developing either FAS 8 or FAS 52. It might be argued instead that some subsequent tax laws followed the financial reporting rules.

In the UK the laws on taxing gains and losses on loan transactions may explain the development of the cover concept in which gains and losses on liabilities are offset by losses and gains on assets. Prior to the mid-1970s there was little reference to foreign currency gains and losses in the UK tax statutes. The issue became important in the mid-1970s when sterling fell 20% against the dollar and even more so against the Swiss franc in 1975. Sterling continued to fall in 1976[110] and the weakened sterling became an issue for companies with foreign borrowings. First of all, UK companies had borrowed much in foreign currencies, particularly the hard currencies such as the dollar and the Swiss franc, in the 1960s and 1970s. The reason for this has been attributed to the UK Exchange Control Act of 1947:

108
Watts and Zimmerman, *ibid.*, 1978.

109
Bryant, *ibid.*

110
Kay and King, *ibid.*

> Permission is required under the Exchange Control Act, 1947 for all payments in sterling or any other currency by United Kingdom residents to non-residents. Thus a United Kingdom resident seeking to acquire overseas investments would be required to acquire currency in the investment currency market (and incur the cost of the premium) or to borrow in foreign currency. The investment premium cost is taken into account, of course, as part of the cost for capital gains purposes, but there is not such recognition in the case of currency borrowings.[111]

Therefore, UK companies would be obliged to borrow heavily in overseas currencies for their foreign operations. Consequently, UK companies were substantially in debt in foreign currency at this time. Secondly, with a decline in sterling these companies incurred a substantial loss on repayment of the debt.[112] But these losses were not tax deductible under the UK income tax law. The tax treatment in the Finance Act of 1965 disallows the gains and losses on repayment of borrowings as taxable or deductible even though borrowings are classified as capital items. The capital gains rules in that Finance Act pertain only to gains realized on disposal of assets, not liabilities.[113]

As a result of pressure from the business community on the Chancellor of the Exchequer to remedy the situation, Inland Revenue published a discussion memorandum, "Borrowings in Foreign Currency" in 1976, outlining the current law and raising questions to consider on changing the law. The Consultative Committee of Accountancy

---

111 Consultative Committee of Accountancy Bodies, TR 209, *ibid.*

112 An example is Beecham Group which borrowed 100 million Swiss francs in 1971 which at current exchange rates equalled 10.13 million pounds. The cost of repaying the loan in 1976 was 22.73 million pounds (Sunday Times, August 8, 1976, cited in Kay and King 1985).

113 Kay and King, *ibid.*

Bodies (CCAB)[114] responded with a memorandum in which they recommended the matching of borrowings with assets: "Tax relief for losses on borrowings which are matched with chargeable assets should be given by way of a capital gains loss. The loss arises only on the repayment of the loan concerned."[115]

ED 21 (1977) labelled this approach the "cover" method which could only be used if the current rate method was used and could not be used if the temporal method was used:

> Under the temporal method fixed assets are translated at historical rates and therefore it is not possible to offset deficits on borrowings denominated in foreign currencies against surpluses arising on fixed assets.[116]

Respondents to ED 21 thought that a global offset of gains and losses on foreign assets and liabilities was imprudent.[117] In ED 27 (1980) the ASC decided to limit the scope of offsets by stating: "..the foreign loan should be denominated in the same currency as that in which the equity investment is denominated."[118] As indicated in the last section,

---

114

Composed of senior officers of the ICAEW, the Institute of Chartered Accountants of Scotland, the Institute of Chartered Accountants in Ireland, the Association of Certified Accountants, the Institute of Cost and Management Accountants, and the Chartered Institute of Public Finance and Accountancy, all in the UK.

115

CCAB, TR 209, *ibid.*

116

The Institute of Chartered Accountants in England and Wales, Accounting Standards Committee, "Exposure Draft 21-Accounting for foreign currency transactions", *Accountancy* 88 (October 1977): 75-79, para. 21.

117

From Appendix 4 attached to discussion papers for ASC meeting held on May 30, 1979.

118

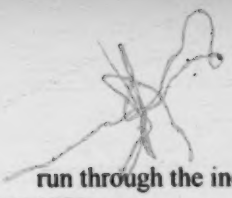
Accounting Standards Committee, *ibid.*, 1980.

commentators opposed this provision on the basis that it was too restrictive. SSAP 20 (1982) offered a compromise by specifying that the offset is permitted only to the extent that the foreign currency borrowings do not exceed the amount of cash expected to be generated by the net investments.[119]

Meanwhile, the Inland Revenue took no action on the tax issue. Instead, a case involving the tax treatment of foreign currency gains and losses, Pattison (Inspector of Texas) v Marine Midland Ltd, came before the High Court in 1981. Marine Midland Ltd borrowed and lent US$15 million from 1971 to 1976. When sterling fell in 1975 and 1976, Marine Midland incurred a 2.5 million pound loss on the debt and a corresponding gain on the loan stock. The Inland Revenue argued that (1) the loss should not be allowed as a deduction because the loan stock was part of fixed capital and (2) that the gain should have been taxed on an accrual basis each accounting period. The High Court agreed with the first argument but not with the second. The liability could only be taxed when the transaction was completed. Both parties appealed but only the company's appeal went before the Court in 1983 and the company successfully argued that the accounts showed no profit or loss because the assets and liabilities were matched. This judgment by the Court supports one of two allowable methods for translating branch accounts for tax purposes in the UK, that is, the 'profit and loss method'. Under that method, the gains and losses are treated as reserve movements (consistent with SSAP 20). The other method, the 'balance sheet method', requires that the gains and losses be

---

[119] Accounting Standards Committee, *ibid.*, 1983.



run through the income statement, concurrent with the current-noncurrent method, which is no longer endorsed in current accounting principles but is available for tax purposes. The Inland Revenue ultimately issued SP 3/85 in 1985 to develop a method of calculating exchange differences that is somewhat consistent with the Marine Midland case.[120]

SP 3/85 was the first attempt to change the tax law in the UK since 1976 when the first memorandum was issued by the Inland Revenue. The ASC issued its pronouncements, from ED 16 up to and including SSAP 20, before the tax law changed; thus it was the old tax law that was in effect which did not permit tax treatment for gains and losses on foreign borrowings. Therefore, given the decline of sterling, there continued to be an incentive to offset the losses on liabilities with gains on assets to keep the gains out of taxable income.

Like the US and the UK, unrealized gains and losses were not subject to tax treatment in Australia according to the 1976 survey.[121] However, unlike the US and the UK, tax treatment for realized gains and losses on foreign currency exchanges in Australia was the same as for ordinary transactions. All capital transactions and loan transactions were taxed or deducted at the ordinary rate, 42.5%.[122] Capital gains

---

120
Kay and King, *ibid.*

121
CCAB, TR 209, *ibid.*

122
Ibid.

legislation was not enacted in Australia until 1986.[123]

The main issue is whether these gains and losses should be included in income. Interestingly, though, submission letters to all of the Australian pronouncements favoured the immediate recognition treatment for gains and losses, at least as much as any deferral or reserve treatment. Only the treatment of losses on long-term monetary items brought about by the declining Australian dollar became an issue when AAS 20 persisted in the deferral treatment and companies supposedly hid huge losses. Prior to 1986 gains and losses were given tax treatment only on those borrowings involving the purchase of trading stock. Those borrowings for the purpose of purchasing a plant or building were exempt from tax treatment for exchange gains and losses. That was changed with the new ruling in 1986 in which exchange gains and losses on all borrowings are now subject to tax treatment. Interestingly, gains on borrowings cannot be offset by losses on sales of related assets (the cover concept in the UK) and vice versa.[124]

As with the other countries, what matters for tax authorities in Australia are the rules that apply to the income statement and not what happens on the balance sheet. In terms of translating the income statement, the law recommends a transaction by

---

123

Richard J. Vann and Ross W. Parsons, "The Foreign Tax Credit and Reform of International Taxation", *Australian Tax Forum* 3 (1986): pp. 202-211. See also R. W. Parsons, *Income Taxation in Australia* (Melbourne: The Law Book Company Ltd, 1985): 424-427, 747-754.

124

Ibid.

transaction approach, analogous to the specific transaction approach in the US. However, in practice, it appears that the Commissioner of Taxation accepts average and year-end exchange rates.[125] The reserve treatment avoids tax treatment for some gains and losses. Until 1986 only certain of these gains and losses were taxable. The losses on borrowings for financial reporting purposes were potentially a greater issue to both companies and users of financial statements than the tax deduction that the losses would have allowed because only those losses pertaining to borrowings for financing trading stock were deductible. The change in the tax law in 1986, which permitted these deductions, just preceded the amendment to AAS 20 in 1987 which disallowed the deferral treatment for gains and losses on long-term monetary items. The result is that more of the losses on long-term debts, which continued to occur because of the falling Australian dollar, were reported on the income statement and were also allowed as a tax deduction. It might be argued that reducing the tax liability provided a greater incentive to amend AAS 20 than the potential of huge write-offs allowed by the reserve treatment. It is not apparent, therefore, whether the tax treatment was the important consideration in the choices made by the Australian standard-setters or the public outcry over the reserve treatment.

In Canada prior to 1972, the Income Tax Act was silent on the issue of treatment of foreign exchange gains and losses for taxation purposes. However, the 1972 Income Tax Act, Section 39(2), which deals with capital gains and losses, was quite vague on

---

125 *Ibid.*

distinguishing whether they should be income items or capital items. It specifies that these gains and losses are capital items only to the extent that they would not otherwise be included in computing income. This distinction is important in Canada because only one-half of the gains and losses on capital items is included in income. They are taxed or deducted at the same rate as ordinary transactions. For loan transactions, the income rate and the capital rate are the same, but again the nature must be determined to know whether one-half or all must be included in the computation of income.[126]

The two main issues are (1) whether the gains and losses are of an income nature or a capital nature and, (2) should they be recognized as they accrue or only when realized (accrual v cash). Due to the lack of guidance in the Income Tax Act on both of these issues, the courts have had to make decisions in this area. By and large, the courts have determined that cases involving inventory purchases are income in nature.[127] The rulings on third-party borrowings are more complex. These gains and losses are generally considered of a capital nature but the courts have considered the use of funds and whether the borrowing represented fixed or circulating capital to the taxpayer. The

---

126

Parkinson, *ibid.*, 1972. Information on tax rates came from The Consultative Committee of Accountancy Bodies, TR 209, *ibid.*

127

Examples of cases are Eli Lilly and Company (Canada) Ltd v M.N.R. and D.W.S. Corporation v M.N.R., and more recently the Northern Sales case, cited in Michael J. White, "Isolated Foreign Currency Transactions and Foreign Exchange Futures Contracts" in *Report of Proceedings of the Thirtieth Tax* Conference, Canadian Tax Foundation, Montreal, 20-22 November 1978, pp. 490-504.

capital nature is overturned if the funds are used in day-to-day trading activities.[128] The timing of recognition is determined by the income versus capital classification, according to court cases. For income items, the taxpayer may choose either the cash or accrual basis but apply the method consistently. For capital items, gains and losses are recognized only when realized.[129]

The CICA pronouncements were consistent in their treatment of gains and losses throughout, except for changing the amortization period from the total life to the remaining life of the item in 1978. The pronouncements recommended the accrual treatment of gains and losses except for those involving long-term monetary items. This treatment differs from the Income Tax Act which requires that a distinction be made between income and capital items, which the CICA recommendations did not. Furthermore, the Income Tax Act did not specify a particular treatment of gains and losses on long-term monetary items, which the accounting pronouncements did. It appears unlikely that current tax laws were the driving factor in selecting the deferral treatment for these items. In fact, the tax laws and the accounting rules are so dissimilar on foreign currency gains and losses that it is hard to determine how one could have affected the other.

Generally, accounting standards for foreign currency preceded tax laws on

---

128

Representative cases include Tip Top Tailor Ltd and Aluminum Union (from White, *ibid.*).

129

See *ibid.* for a discussion of representative cases.

foreign currency gains and losses in these countries. Tax laws could have affected the development of accounting standards only if tax authorities were deliberating on them prior to or concurrent with the deliberations on accounting standards. The evidence suggests that this was not the case. Therefore, the effect of tax laws on accounting standards for foreign currency, for either the differences or the consensus of methods and treatments, appears to be minimal.

V. Conclusion

The comparative analysis in this chapter follows the strategy begun in the previous chapter by presenting evidence that shows that certain plausible factors or conditions that could explain the choices made by standard-setting bodies only partially explain the actual choices made. The focus of this chapter is the possible effects of extant reporting practices, accounting principles, corporate lobbying, and tax laws on choices of methods for foreign currency accounting.

Collectively, these factors do explain some of the methods and treatments endorsed by standard-setting bodies. The predominate application of the current rate method in the UK and Australia would explain its endorsement by standard-setters in these countries. The current rate method was also the method preferred by the majority of lobbyists in Australia. This method might also be endorsed by some UK lobbyists because of the more favourable results of applying the current rate method during inflationary periods. Because inflation was lower in the US in the early 1970s and

because of an adherence to historical cost principles, the temporal method was favoured by US standard-setters. Maintaining historical cost might also explain the preference for the temporal method in some of the pronouncements in Canada and Australia. However, the resistance to the temporal method in the late 1970s, specifically in the US, might be explained by the combination of increased inflation and a tax liability that the method produced.

In terms of treatment of gains and losses, the all-inclusive income concept is credited with explaining the preference at times among these standards-setters for immediate recognition in the income statement. However, in times of devaluing currencies, deferral methods or balance sheet treatments, which were endorsed in Australia when the Australian dollar fell, would be preferred. Lobbyists' responses indicate that deferral was the preferred treatment in the mid-1980s but this may also be due to the change in the tax laws at that time which subjected exchange gains and losses to tax treatment. The immediate recognition treatment might also be tolerated more in the UK, in spite of falling sterling, high inflation, and current tax treatments, because of offsets under the cover concept, which was not endorsed in Australia. This treatment might also have been endorsed in the US when inflation was low but lobbyists resistance to the income statement treatment appeared when inflation increased in the US.

Current practice may explain the endorsement of the current rate method and accounting principles may explain the endorsement of the temporal method in the early pronouncements. However, neither of these explanations were adhered to in the final pronouncements that were issued in which both of these methods were endorsed. The

material presented in this chapter would suggest that if standard-setting bodies developed standards based on current practice, the US and Canada would have permitted a number of different methods, the UK would not have considered the temporal method, and Australian standards would not have wavered back and forth between methods. The standard-setters in the UK and Australia would have endorsed only the current rate method and not necessarily the temporal method if their choices reflected current practice. The current rate method was eventually the primary method endorsed in the consensus that evolved.

Support for the temporal method was not based on current practice, but it was endorsed initially as the preferred method in some jurisdictions and later for certain conditions in the final standards. The temporal method was shown to have some conceptual appeal because it retained the historical cost principle but the consideration of this and other accounting principles was not uniform among the countries. The current rate method appears to have less conceptual appeal but is favoured because it retains values in translation, which lends some support for the preference for the current rate method. However, it does not explain how the temporal method is best suited for operations in which foreign subsidiaries are but an extension of the parent company. It is not clear why the retention of historical cost is applicable in those circumstances and not others. The endorsement of both the current rate method and the temporal method in certain conditions suggests a contradiction where the historical cost principle is concerned. The endorsement of both methods suggests that the application of accounting principles had less influence than other factors in these endorsements.

The debate over treatment of gains and losses appears to reflect a struggle between certain accounting concepts and some other factors, but not necessarily current practice. In all cases, current practice for treatment of gains and losses was quite varied and standards would have allowed many different methods if current practice had been the basis for the prescribed treatments. As the analysis indicates, current practice can only partially explain the choices made for translation method and treatment of gains and losses, whether considering the differences in the early standards or the consensus that followed. Standard-setters were divided on the treatment of gains and losses, citing the all-inclusive income principle as the basis for the income statement treatment in the US and the UK. Until consensus was reached on this topic, the standard-setters in Australia and Canada endorsed deferral, especially on long-term items. It is difficult to attribute the application of an accounting principle or principles to either deferral or reserve treatments. As with translation methods, the consensus that was reached on treatment of gains and losses permits both methods under certain circumstances. It is not clear how the all-inclusive income principle is relevant in some circumstances and not in others. As with current practice, the consideration of accounting principles played a role in the choices made but do not fully explain them. At best, current practice and accounting principles can explain some of the differences that existed in the early standards but not all. Also, neither of these factors explains how the temporal method fell out of favour but was later endorsed for specific circumstances.

One of the similarities of the standard-setting process in these countries is the opportunity for constituents to lobby for preferences in accounting provisions. This

chapter presents lobbying efforts in the form of comment letters (or submission letters as they are called in Australia). In the case of accounting for foreign currency, standards do not completely reflect the majority preference for translation method or treatment of gains and losses. Previous research would suggest that US and UK standard-setters would have not endorsed the income statement treatment if they were following the majority view of lobbyists. Canadian standard-setters had no majority opinion from lobbyists on either translation method or treatment of gains and losses and therefore, anything they endorsed, except for tolerance of all methods, would reflect lobbyists' opinions. Australian respondents consistently endorsed the current rate method and the income statement treatment for gains and losses but as the analysis indicated, the Australian standard-setters switched back and forth in prescribing methods and treatments. One of the interesting results of the analysis is that the final standards that reflect a consensus contain provisions and methods that were not articulated in the comment letters by lobbyists. This is not to say that lobbying efforts through comment letters had no influence on standard-setters choices, but the incongruence between majority opinion and the final results suggests that lobbying efforts were only partially influential in developing standards for foreign currency accounting.

The comparative analysis also indicates little support for the tax considerations in developing standards for foreign currency accounting. Generally, the tax laws were developed after the accounting standards and in some cases the accounting standards provided the basis for the tax laws.

The factual material in each case demonstrates the unlikelihood that current

practice, accounting principles, currency fluctuations, lobbying efforts, or tax laws explain the choices for translation method and treatment of gains and losses. The analysis suggests that these factors are insufficient in explaining the preference for certain methods of foreign currency accounting by different standard-setting bodies and how they moved towards consensus. While the comparative analysis is helpful in putting into perspective some of the plausible explanations for the different choices of methods and treatments, a study of social nature of the process involving power and networks of alliance among the parties involved, including interrelationships among the standard-setting bodies themselves, provides a more complete view of this complex process.

CHAPTER 4. THE ROLE OF POWER IN SETTING FOREIGN CURRENCY STANDARDS

The purpose of this chapter is to further examine the development of standards for accounting for foreign currency, taking into account the effects of conflict among specific entities over the final outcomes and the impact of certain social discourses in these developments. The chapter extends the argument of the previous chapters for the choices made by standard-setting bodies in the US, the UK, Australia, and Canada in developing these standards. Initially, significant differences existed in the standards. Therefore, one of the questions being addressed here is why do different social entities facing a task (of establishing a set of accounting rules for the effects of floating exchange rates) develop different approaches to the issue? At the same time, why would accounting standard-setting bodies with existing investments in standard-setting in different countries realign their commitments to pursue harmonization? The answers to these questions involve a study of power which is addressed in this chapter.

The accounting literature recognizes that certain powerful individuals and groups have influenced the development of specific standards.[1] Studies of power in standard-

---

[1] Anthony Hope and John Briggs, "Accounting Policy-Making: Some Lessons from the Deferred Taxation Debate", *Accounting & Business Research* (1982): 83-96; Anthony Hope and Rob Gray, "Power and Policy Making: The Development of an 'R & D' Standard", *Journal of Business Finance and Accounting* (1982): 83-96; M. E. Hussein and J. C. Ketz, "Ruling Elites of the FASB: A Study of the Big Eight", *Accounting Review* (1980): 354-367, cited in Robson and Cooper, *ibid.*

setting[2] emphasize a perspective of power similar to the pluralist view of power in which the entity with power is identified by outcomes of particular situations and by relating these outcomes to actions of the powerful.[3] In emphasizing the pluralist approach to the standard-setting process in lobbying studies[4] there is an implicit assumption that individual firms have the potential for influencing the process. Under pluralism, power is measured by the differences in the ways individuals respond to the exercises of power to which they are subject.[5] Similarly, the lobbying activities are studied for the purpose of predicting the consequences of accounting policy changes, such as circumventing reporting requirements, subverting the standard, and/or discrediting the policymaker. Conflict is assumed in this model and also in lobbying studies as the studies are posited to assist the standard-setting agency in assessing potential opposition to a standard.[6] Conflict can also exist between lobbyists.

2

J. R. Haring, "Accounting Rules & 'The Accounting Establishment'", *Journal of Business* (1979): 507-520; Hussein and Ketz, *ibid.*; Hope and Briggs, *ibid*; Hope and Gray, *ibid.*

3

Robert A. Dahl, "The Concept of Power", 2 *Behavioral Science* (1957):201-205; "A Critique of the Ruling Elite Model", *American Political Science Review* 52 (1958): 463-469; *Who Governs? Democracy and Power in an American City* (New Haven and London: Yale University Press, 1961).

4

For a review of studies on foreign currency accounting, see Houston, *ibid.* For examples of lobbying studies on foreign currency accounting, see Griffin, *ibid.*, 1982 and 1983 and Kirsch, *et al.*

5

Robson and Cooper, *ibid.*

6

Kelly, *ibid.*, 1985.

In the elitist view of power, consideration is given to the idea that certain issues may not be acted upon because the agenda is controlled by those in power.[7] In pluralist analyses, the focus is on *observable* conflict in the process of decision-making over overt key issues. The elitist view considers the possibility that outcomes and interests are not causally linked, that agenda-setting may be present in view of the potential conflict between constituents and standard-setting bodies. This view of power recognizes that conflicts outside of the decision-making arena can lead to non-action in the political process through the effect of an elite group controlling the agenda for decision-making.[8]

Finally, in the link between outcomes and interests the possibility exists of mistaken calculations of interests or that interests are discursively formed, that is, that actors, in calculating their own "interests" may draw upon certain social discourses in order to influence a specific process.[9] Furthermore, the processes of persuasion and other possible techniques are used by groups to persuade those in power to align with

---

7

Lukes, *ibid.*; P. Bachrach and M. S. Baratz, "Decisions and Non-decisions: An Analytical Framework" *American Political Science Review* (1963):641-51; and Bachrach and Baratz, *Power and Poverty: Theory and Practice* (Oxford: Oxford University Press, 1970), cited in Lukes, *ibid.*

8

In the elitist view of power, power is "exercised when A devotes his energies to creating or reinforcing social and political values and institutional practices that limit he scope of the political process to public consideration of only those issues which are comparatively innocuous to A". From Bachrach and Baratz, *ibid.*, 1970. A typical example of this view of power is the practice of political organizations in which certain potentially harmful (to A's power position) items are excluded from meeting agendas.

9

Robson, *ibid.*, 1993.

their interests.[10] This radical view of power[11] builds on both the pluralist view and the elitist view by considering power effects in which one entity or individual exerts power over another in ways that persuade the other entity to identify its interests with that of the first party and that certain interests may become prevalent over other interests through processes of socialization and/or ideologization.

Robson's study of translation in the formation of the Accounting Standards Steering Committee [12] focuses on the emergence of accounting change in terms of the process of translation between non-accounting discourses and rationales and the problematization of accounting techniques. The objective of that study "was to elaborate a set of conceptual instruments or devices for the investigation and theorization of accounting change."[13] Robson states: "...it was argued that it is necessary to attend to the process through which particular accounting statements, calculations and techniques are subject to a translation in wider social, economic and political discourses not normally associated with the apparently neutral, technical discourse and practices of accounting."

While the wider social, political and economic discourses "stimulate the process

---

10

Lukes, *ibid.*

11

Ibid.

12

Keith Robson, "On the Arenas of Accounting Change: The Process of Translation", *Accounting, Organisations and Society* 16 (1991): 547-570.

13

Ibid., p. 565.

of accounting change"[14], the outcome of these changes is not necessarily only the result of such discourses. The outcome is also influenced by the formation of network alliances on the part of specific political actors. In power relations possibilities exist for resistances and reversals which can affect the result of any political process.[15] Players often act in ways to legitimate their existence and will form alliances which bear on the outcomes of such processes as accounting standard-setting. These alliances are under-emphasized in investigating the development of accounting standard-setting. The potential opposition by constituents at large is overemphasised when seen in the context of specific alliances which have a greater influence on the outcome of standard-setting deliberations. This idea lends support to the institutional theory that participation in the standard-setting process via lobbying serves merely to ensure the legitimacy of the standards and the standard-setting process but have little bearing on the final outcomes of that process.[16]

This dissertation studies the actions of specific actors that influenced accounting

---

14

Ibid.

15

An example of resistance to US accounting methods is the refusal by the IASC and non-US countries to adopt the last-in, first-out method of inventory, one of the most popular methods among US companies.

16

P. R. Tandy and N. L. Wilburn, "Constituent Participation in Standard-setting: The FASB's First 100 Statements", *Accounting Horizons* 6 (1992): 47-58 and S. B. Johnson and D. Solomons, "Institutional Legitimacy and the FASB", *Journal of Accounting an Public Policy* 3(2) (1984): 165-183, cited in Sara York Kenny and Robert K. Larson, "The Development of International Accounting Standards: An Analysis of Constituent Participation in Standard-Setting", *The International Journal of Accounting* 30 (1995): 283-301.

development through a process of developing alliances with standard-setting bodies. As Robson suggests, "a final outcome can be 'worlds apart' from initial causes or origins".[17] To understand accounting change not only requires knowledge of the origins of the change, but also how the outcomes evolved. To neglect this process leads to misjudgments concerning the perceived level of cooperation among standard-setting bodies internationally,[18] taking into consideration only the actions and outcomes of the bodies themselves and under-emphasizing the role of other actors that influence the process. In the case of foreign currency accounting, accounting change was stimulated by political and economic conditions that resulted from a floating exchange rate system. This change in the political economy had implications for accounting change. By analysing the development of foreign currency standards, one can potentially identify the ways in which the difficulties of harmonization are embedded, not in cultural differences or even differences in accounting approaches among countries, but rather in processes involving entities with specific preferences for accounting methods. These entities are not easily categorized by country affiliation or any other classification.

Given this perspective concerning networks of alliance, a study of observable conflict is relevant for the investigation of the development of foreign currency standards. Conflict among various constituents in this process is very evident and

---

17

Robson, *ibid.*

18

See Kirsch and Becker-Dermer for a discussion of consensus where foreign currency accounting is concerned.

suggests that various actors actions and expressed interests characterize the process of these developments in formulating account policy. Much of this dissertation emphasizes this perspective of power in understanding how foreign currency standards were developed, thereby helping to explain how the specific methods and treatments were chosen by the standard-setting bodies and filling in some of the gaps left by the analysis in Chapters 2 and 3 concerning the conditions or factors that might be offered to explain these outcomes.

However, one cannot limit the thought concerning the role of power to just that perspective alone. While there was virtually no evidence to suggest that agenda-setting or the exclusion of certain interests was part of the process of developing foreign currency standards, the possibility exists that interests or preferences by some entities did not enter the decision-making arena. Only a few MNCs were influential in this process. That begs the question of why were these preparers so involved in the process and not others. Was it perhaps that these particular entities were viewed as "experts" in the area of accounting for foreign currency transactions, or were there other factors at play?

The view that power is exerted through discourse and the influence of certain ideologies also has relevance for the understanding of the development of accounting standards. The notion that the purpose and objective of accounting information is for decision-making by investors and creditors was also being developed at about the same time that foreign currency standards were put on the agendas of standard-setting bodies. This viewpoint would signal to the world at large that other entities would not have an interest in the results of deliberations concerning foreign currency standards because the

overall benefit of standards is limited to investor/creditor interests and that specific methods and treatments are neither here nor there for anyone else. In actuality, however, there is very little interest shown on the part of investors and creditors in these deliberations, indicating perhaps that standard-setting has relevance only for preparers of financial statements and not anyone else in particular.

This then brings us back to the view of power in which observable conflict and outcomes of the process become the focal point of this study. If entities that may have an interest in financial statements perceive them as relevant for investors and creditors only, if investors and creditors show little interest in the development of standards, if only a few companies exert an influence in this process, then what is left is the examination of actions and expressions of these few entities as they relate to the final outcomes of the standards. This analysis helps to explain the choices made by the standard-setting bodies in the development of foreign currency standards.

The first part of the chapter presents a discussion of theories of power involving Lukes' three dimensions of power and Gaventa's study of quiescence. The second part of the chapter is an analysis of the relations between the standard-setting bodies and outside parties that affected the efforts to harmonize and demonstrates the significant effects of networks in the process of accounting regulation. The third part of the chapter presents evidence of efforts toward harmonization of foreign currency accounting by the standard-setting bodies in these countries and how various discourses played a role in this development.

The strategy in the second section entails identifying interactions between

standard-setting bodies and/or task forces on foreign currency with MNCs and other interested parties. The correspondences, meetings, and other actions by these groups are examined to identify how the interests of standard-setting bodies were aligned with the interests of a select few MNCs. Where evident, the resistances by standard-setting bodies or opposing groups are noted and shown to also play a part in developing the standards in each of the jurisdictions under study. The standard-setting bodies that are investigated include the FASB in the US, the ASC in the UK, the AARF and the Accounting Standards Research Board (ASRB) in Australia, the CICA in Canada, and the IASC.

The case study method employed here is relevant for understanding the role of power in developing foreign currency standards. The case study method permits an opportunity to study this process of developing a standard in detail, and thereby allowing an examination of the multiple interactions involved. The small sample size does not permit the implementation of statistical analysis. Rather, the examination through the case study method allows the means by which in-depth examination of the interactions between standard-setting bodies and MNCs and among themselves can be conducted. To understand the differences in the methods and treatments endorsed by the standard-setting bodies in the four countries and the IASC and how these bodies moved towards consensus requires an examination of the actors' decisions and what influenced or lead to those decisions, which can best be achieved by examining the process in such detail in a way that cannot be captured as well by experimental methods. Furthermore, the intent of the study is not to model the process for prediction purposes but rather to gain a better

understanding of the process itself.

Sources of information for this study include, where available, minutes of meetings, letters, news releases, issued pronouncements, task force memoranda, and other relevant documents of these standard-setting bodies that concerned the foreign currency standards. This information was gathered from the offices of the FASB, the ASB, and the AARF with the expressed permission of library staff in charge of archival material. Some information was gathered through interviews with people who served on the task forces. Other information was obtained from books, one of which was written by a former staff member of the FASB, the other written by a current staff member of the AARF.

Information is rather limited from the CICA and the IASC because of rules concerning confidentiality. Minutes of meetings and other documentation were not publicly available from the FASB before 1979, the CICA, or the IASC. Many of the standard-setting bodies did not permit public scrutiny of minutes of meetings or any other documentation during the time period under study. As a result, there was no access to FASB minutes prior to 1979. Two attempts were made to obtain information from the CICA. Both the librarian and David Moore expressed the sentiment that public scrutiny of CICA minutes, letters, or other memoranda were not available. Only articles on foreign currency translation from published journals were available from the CICA. Minutes of IASC meetings concerning foreign currency standards were inadvertently discovered at the office of the AARF in Australia, but given the IASC policy on confidentiality it was deemed by this author that it would be unethical to examine and

report on the findings from those minutes. Therefore, the evidence from these organizations is mainly based on information gathered from interviews and information from secondary sources.

The limitations of relying on these data sources is that telephone conversations which quite likely occurred are not on record. Furthermore, the actual testimonies of individuals at public hearings is not on record. The investigation for this dissertation occurred not during the process of developing the standards but many years later. Thus, not all interactions between task force members and other interested parties can be analyzed. Interviews were conducted and transcripts of interviews conducted by other people were examined to alleviate some of these difficulties. In the end, however, one must rely on the memories of people about a situation that occurred some time ago. Nevertheless, the interview material did reinforce the preferences and the involvement of the particular MNCs in this process.

The analysis in the third section of this chapter entails identifying discursive conditions from which emerged the possibility for regulating foreign currency accounting. These include the discourses concerning the harmonization of accounting standards in general. This in turn affected the outcome of a new accounting technology, foreign currency accounting. The evidence for this section includes journal articles reporting speeches of those advocating harmonization and examining how the authors drew upon certain discourses of the time to justify their view.

I. Theories of Power

Concepts of power that are applied in this study to the development of accounting standards for foreign currency translation are considered relational and involve conflict. This relational perspective of power seeks to understand how different things, viewpoints, people, etc., are brought together and how differences and similarities are constructed and maintained.[19] For international accounting research, this entails the investigation of how members of different social worlds come together to practice a common approach to accounting practice through the development of standards. The study of the development of foreign currency accounting standards in this dissertation involves understanding the nature of the relations that ultimately affected the methods and treatments for foreign currency accounting and the extent to which harmonization was achieved.

This perspective contrasts with facilitative views of power which involve the use of authoritative decisions to further collective goals.[20] Conflict of interest is not present

---

19

John Law, "Introduction: monsters, machines and sociotechnical relations", in John Law (ed.), *A Sociology of Monsters: Essays on Power, Technology and Domination* (London: Routledge, 1991a): 1-23.

20

Talcott Parsons, "The Distribution of Power in American Society", *World Politics* 10 (October 1957): 123-143; "On the Concept of Influence", *Public Opinion Quarterly* 27 (1963a): 37-62; "On the Concept of Political Power", *Proceedings of the American Philosophical Society* 107 (1963b):232-262; *Sociological Theory and Modern Society* (New York: The Free Press, 1967); Hannah Arendt, *On Violence* (London: The Penguin Press, 1970), cited in Lukes, *ibid.* Also, A. Giddens, *New Rules of Sociological Method* (London: Hutchinson, 1976); *Studies in Social and Political Theory* (London:

in concepts of power in which power is seen as the ability to achieve goals.[21] In these views, power is a capacity or ability, not a relation. "With that disappears the central interest of studying power relations in the first place--the securing of people's compliance by overcoming or averting opposition."[22] The evidence on the development and harmonization of foreign currency standards suggests that overt conflict and measures to avert potential sources of conflict were part of the process. However, the perspective on power in this study is less structuralist than Marxist views on power. The latter position would suggest that interests correspond to class positions, a view which under-emphasizes other sources of conflict and therefore excludes other modes of interest representation.[23]

The one-dimensional view of power is relevant to the development and harmonization of foreign currency standards. This view of power is based on Dahl's concept in which "A has power over B to the extent that he can get B to do something that B would not otherwise do."[24] In this view, the exercise of power is the crucial point. Not only does A have the capacity of power, it has been successfully exercised. For

---

Hutchinson, 1977); *Central Problems in Social Theory* (London: Macmillan, 1979); *A Contemporary Critique of Historical Materialism* (London: Macmillan, 1981); *The Constitution of Society* (Cambridge: Polity Press, 1984), cited in Clegg, 1989, *ibid.*

21 Lukes, *ibid.*

22 *Ibid.*

23 Clegg, *ibid.*

24 Dahl, *ibid.*, 1957.

researchers studying power, the focal point is observable behaviour in the course of decision-making. Those who prevail in decision-making are those with power. Another key element is actual and observable conflict, which is necessary to assess which decisions run counter to other decisions and which decisions prevail. Conflict in this view is between preferences. It is assumed that preferences are exhibited in actions and are discovered by observation of actors' behaviour. It is also assumed that interests are revealed by preferences. This view does not allow that interests might be unobservable or that actors might be mistaken about their own interests or how action might affect their interests.[25] The involvement of certain MNCs in the process of developing foreign currency standards demonstrates this perspective on power. Different preferences for specific methods of translation and treatments of gains and losses were evident throughout the debate concerning these methods and treatments.

Bachrach and Baratz[26] criticized Dahl's approach as too restrictive and developed the two-dimensional view of power. While recognizing the legitimacy of the one-dimensional view, they added that "power is also exercised when A devotes his energies to creating or reinforcing social and political values and institutional practices that limit the scope of the political process to public consideration of only those issues which are comparatively innocuous to A."[27] Their work brings to the forefront a notion of

---

25
Lukes, *ibid.*

26
Bachrach and Baratz, *ibid.*

27
Ibid.

"mobilization of bias", which means that political structures operate in such a way as to organize certain issues into politics, and organize certain other issues out, for the benefit of certain groups and at the expense of others. So while power is evident by certain decisions being made, it is also evident by certain decisions not being made. Power is exercised by confining the scope of decision-making to "safe" issues. Decision is a choice of alternatives while non-decision is a decision that represses challenges to interests of the decision-maker. The result of the exercise of nondecision-making power is that challenges to the status quo are killed before they reach the decision-making arena. As in the one-dimensional view, a significant feature is conflict, but in the case of the two-dimensional view, the conflict may be either overt or covert; covert in the sense that conflict still exists even though challenging issues are not brought to the decision-making arena because the conflict exists outside of that arena. Conflict that is covert is between the interests of those engaged in the nondecision-making and the interests of those excluded from the decision-making arena. As in the one-dimensional view, the emphasis is on observable behaviour, as Bachrach and Baratz assume that the latters' interests are also observable;[28] thus power must be actualized, and is not merely a capacity.

Criticisms of the two-dimensional view include difficulty in identifying the existence of the covert conflict of interests. Furthermore, some nondecisions may be part of unconscious routine or a decision to abstain from being involved in a decision. Other

---

[28] Lukes, *ibid.*

nondecisions may be due to non-participation because of an unawareness of people's interests so they are not in a position to demand that their interests be satisfied.[29] This last point is relevant for the development and harmonization of foreign currency standards in that groups or entities that might have had a interest in the outcomes of the process did not directly participate in the process. This perspective, however, emphasizes activities that thwart this participation by controlling the agenda. The evidence on foreign currency standards does not reveal much in the way of activities that controlled the agenda for developing these standards. That is not to suggest that such activities did not occur, but as stated earlier, empirical evidence to suggest that they did occur is difficult to provide.

Lukes criticizes the commitment to actual, observed behaviour in the two-dimensional view. He argues that those who defend the status quo and control the political agenda may be unaware of the existence of potential challengers because their control may be so pervasive. Secondly, Lukes criticizes the emphasis on actual, observable conflict. Conflict is not necessarily inherent when power is exercised through manipulation and authority. Furthermore, the notion that power is only exercised in situations involving actual and observable behaviour is too limiting. In Lukes' view, A not only exercises power over B by getting him to do what he would not otherwise do, but also exercises power over B by influencing, shaping, or determining B's wants.

---

[29] R. E. Wolfinger, "Nondecisions and the Study of Local Politics", *American Political Science Review* 65 (1971a): 1063-80, and "Rejoinder to Frey's Comment", *American Political Science Review* 65 (1971b): 1102-04, cited in Clegg, 1989, *ibid.*

"Indeed, is it not the supreme exercise of power to get another or others to have the desires you want them to have--that is, to secure their compliance by controlling their thoughts and desires?"[30] Through mass media and other means, leaders shape the preferences of their constituents. Lukes is adamant about the fact that Bachrach and Baratz ignore a crucial point that the greatest use of power is to prevent conflict from arising in the first place. Also, there is the problem of observed grievances. In the two-dimensional view of power, it is assumed that if there are no grievances, then there are no interests that are not satisfied. Defining and observing a grievance is problematic but also there is the fallacy of believing that the absence of grievance equals a consensus which rules out the possibility of false or a manipulated consensus.

Lukes' three-dimensional view of power involves the ways in which issues are kept out of politics which can occur in the absence of actual, observable conflict. The conflict in this view is latent and consists of conflict between the interests of those exercising power and the real interests of those who are excluded from the decision-making arena. Those who are excluded may not express or even be aware of their real interests. The conflict is latent in the sense that it would be observable if the excluded group were to become aware of their real interests.[31]

An empirical study of three-dimensional view of power would provide evidence of the ways in which As prevented certain interests of Bs from being acted upon or the

---

30 Lukes, *ibid.*,p. 23.

31 *Ibid.*

ways in which As promoted other interests. The first step is to justify what Lukes calls the "relevant counterfactual". In this step, one must establish an implicit value judgment of some choice of action or situation and then develop a testable hypothesis that the interested parties did indeed prefer that situation. An additional task is to compare a similar group facing the same choices but where power relations were not operative to determine whether that group was able to choose the preferred action or made the choice with less difficulty. The difficulty here is assuming that the Bs in question would indeed have made the preferred choice had there not been the influence of As. This problem makes it difficult to draw conclusions regarding the alleged influence of A over B. The second step is to identify the mechanisms or the processes of this alleged exercise of power. Some of these may be identified as inactions. For this to be observable, it must be established what the consequences would be as result of inaction or identifying a consequence that did not occur that would have if action had taken place.

Obviously, these consequences are not always clearly identifiable. This leads to questions such as, was it in the "real interest" of standard-setting bodies or MNCs to effect international harmonization of standards for foreign currency accounting? Real interests are difficult to conceptualize. Habermas argues that only in "ideal speech situations", in which "individuals are unconstrained in their ability to participate in any discourse on conditions of their own existence", will real interests be revealed. Power acts as a barrier to free, undistorted communication and, thus, to achieving truth or

enlightenment.[32] The problem is trying to identify a condition in which communication is not distorted,[33] analogous to Lukes' relevant counterfactual. Underlying Lukes' radical view is the notion that without B's autonomy and democratic participation, A determines what B's interests really are or should be and exercises power on the basis of that judgment. Real interests will only be expressed in an appropriate counterfactual condition but an outside observer has to judge how the actor would behave under that hypothetical situation.[34] Judgment by an outside observer is made against a standard of real interests or may be made capriciously or inconsistently. If the subject makes the judgment, it is "impossible to differentiate an authentic, real articulation of interest, which is made from 'without power', from an unauthentic, false articulation of interest, which is made as a result of the constraints of power".[35] Subjects are assumed to know their own interests and can articulate them without compromising themselves in some way.

Foucault sees power as a "more or less stable or shifting network of alliances

---

32

J. Habermas, "Toward a Theory of Communicative Competence", *Inquiry* 13 (1970): 360-75; *Knowledge and Human Interests* (London: Heineman Educational Books, 1972); *Legitimation Crisis* (London: Heineman Educational Books, 1976), cited in Clegg, *ibid.*

33

Clegg, *ibid.*

34

T. Benton, "'Objective Interests and the Sociology of Power", *Sociology* 15(2) (1981):161-84, cited in Clegg, *ibid.*

35

Clegg, *ibid.*, p. 100.

extended over a shifting terrain of practices and discursively constituted interests".[36] Foucault attempts to show how agency and structure are constituted through discourse.[37] Interests, too, are discursively formed. Foucault is not interested in the truth or falsehood of discourse, but rather how discourses have been constituted historically. This relates specifically to Lukes' three-dimensional view--what are the discursive techniques used by A to align B's interests with A's? For this dissertation, the task becomes one of identifying how discourses[38] affected the development of foreign currency standards. Again, that entails the concept of real interests. As indicated, the imputation of real interests is problematic.

Gaventa offers a way of circumventing the problem of identifying real interests. He dispenses with the notion of real interests and modifies the three-dimensional model. In his study, there is no reference to interests. Rather, the processes of myth-building, persuasion, legitimation, and ideologization take precedence. Identifying real interests, according to Gaventa, is not required to study power relations. What is necessary is to show that B is prevented from acting upon certain posited interests and the act of prevention on A's part is sufficient to show that the interests that are expressed by B are

---

[36] Clegg, *ibid.*, p.154.

[37] Clegg, *ibid.*

[38] Discourses in this study include forms of communication such as spoken and written comments, speeches, letters, written articles, and books on the topics of foreign currency accounting and harmonization in general and also written documentation concerning the role and purpose of accounting information and the standard-setting boards.

probably not B's real ones.[39]

Gaventa's study of the Appalachian Valley sought to answer the question of why did the people of the Valley not rebel against the oppressive conditions wrought upon them by the mining companies, i.e., how did power relations maintain the high degree of quiescence observed in these communities? A similar question might be asked concerning the quiescence by nation states, local interests in accounting, and national standard-setting bodies in relation to accounting harmonization. In other words, why would these bodies acquiesce to a world-wide, harmonized system of accounting which would take away their authority and ability to regulate accounting in their own jurisdictions? These groups developed national rules initially and then acquiesced to world harmonization.

In spite of the drawbacks of the methodology discussed in Lukes, the empirical approach has relevance for the study of the choices made by standard-setting bodies in developing standards for foreign currency accounting. In previous chapters, it was established that the various factors such as current practices, application of accounting principles, currency movements, tax laws, and lobbying efforts do not fully explain the choices made. The key to the argument are the assumptions that the act of developing standards was in the interests of parties involved and that international harmonization had value to these parties in view of the difficulties associated with conducting global business in an environment with different accounting systems. These assumptions are

---

[39] John Gaventa, *Power and Powerlessness: Quiescence and Rebellion in an Appalachian Valley* (Urbana, Ill.: University of Illinois Press, 1980).

necessary for setting up the counterfactual situation. The hypothesis that businesses, accountants, investors, and regulators would prefer harmonization is indeed plausible given their value judgments.

The value judgments of these actors is examined through a study of the role of discourse concerning international harmonization. In this study of standard-setting for foreign currency accounting, what is apparent is an initial lack of consensus on the part of standard-setting bodies in light of an assumed interest in international harmonization which later developed into a consensus. The part of Gaventa's methodology that can apply to the standard-setting process is identifying the processes of socialization concerning harmonization and arguing that the discourses on this more general subject affected the development of foreign currency standards.

In this study the approaches discussed in Dahl, Lukes, and Gaventa apply to the development of foreign currency standards. In the next section of this chapter, Dahl's one-dimensional view of power is represented by the conflict among MNCs involved in the deliberations over methods and treatments. The three-dimensional view also applies. From Lukes comes the strategy of justifying the relevant counterfactual to establish that harmonization was in the "interests" of the standard-setting bodies, i.e., that the standard-setting bodies did indeed express an "interest" in harmonizing foreign currency standards. The third part of this chapter investigates how it came to be that interests in harmonizing accounting standards developed. The translation of ideas concerning harmonizing accounting standards to facilitate capital flows is part of the basis for the direction taken by the standard-setting bodies. Gaventa's strategy of identifying the

discursive processes that socialized not only standard-setting bodies but all interested parties toward harmonization is also presented in that section.

II. The Role of MNCs in Developing Foreign Currency Accounting

The evidence in previous chapters of this dissertation suggest that there is little congruence between the majority views on foreign currency standards and the final provisions of these standards. The following account of the development of foreign currency standards describes overt conflict involved in the process and emphasizes the participation and effects of a few MNCs. This account questions the perspective in accounting literature which attempts to determine or predict the preferences for accounting methods and techniques by studying the preferences expressed in comment letters by constituents at large. This section argues that to examine only the perspectives of the constituents at large overlooks the effects of those few entities that position themselves to exert power in the situation. While this point may not be generalized to the development of all accounting standards, it does apply to the development of foreign currency standards. The final standards were based on the preferences of a couple of MNCs which argued for their preferences based in part on their unique situation of having parent companies in two countries, a situation that is not common for all MNCs. Yet their preferences "won out" over those of other MNCs which argued for other provisions based on their own unique situation. This evidence suggests that to understand the processes involved in standard-setting entails a study of the conflicts

involved among the entities which choose to influence the process. From this examination one might gain an understanding of the difficulties involved in international harmonization rather than attribute these difficulties to general characteristics such as cultural differences among countries.

A crucial part of this study is the directions taken and choices made by standard-setting bodies in view of the expressed interest in harmonization and the initial lack of a consensus concerning foreign currency standards among the parties involved which eventually did reach a consensus. The contention of this dissertation is that the outcomes of this series of events was a result of a process involving networks of alliances and that neither the consensus nor the lack of it was a result of differences among the countries concerning national practices at the time, accounting principles, lobbying, tax laws, or currency fluctuations, or even similarities concerning approaches to accounting standard-setting.

The beginning of the flexible exchange rate system and the ideology concerning accounting standard-setting and harmonization may explain the interest shown in developing standards for foreign currency accounting. However, these are insufficient to predict the outcome of actions taken by individual standard-setting bodies. The development of accounting standards involves not only the standard-setting bodies but also the users of financial statements and other parties affected by them. Latour states that the fate of a technology depends on others' behaviour.[40] Therefore, it is necessary to

---

[40] Bruno Latour, *Science in Action* (Cambridge, MA: Harvard University Press, 1987).

examine the responses to the development of a technology (accounting standards are viewed here as a technology) and how the technology is modified, strengthened, and undermined in its development and implementation.[41] This development includes the resistances exhibited by parties in opposition to the technology. Resistance is not considered negative in this process, but rather a means for redefinition and refabrication of the technology.[42] This study examines how the political and economic conditions of the late 1960s and early 1970s and the concern over fluctuating exchange rates became translated into developing and harmonizing accounting standards for foreign currency.

Each of the countries in this study has its own history and its own variations in local factors (currency fluctuations, tax laws, interpretations of accounting principles, current practice, and lobbying effects) which had an influence on the interpretation of what accounting for foreign currency should be. Accounting for foreign currency had a different meaning in each of the jurisdictions in this study and went through a variety of processes which are the result of differing actor-networks and alliances. The actor-networks were closely linked, however, and, in the end, produced a consensus of accounting methods. This result is due to the major role that a few specific MNCs played as actors in this network. This section of the chapter analyses the alliances between standard-setting bodies and these MNCs.

41

Alistair M. Preston, David J. Cooper, and Rod W. Coombs, "Fabricating Budgets: A Study of the Production of Management Budgeting in the National Health Service", *Accounting, Organisations and Society* 17 (1992): 561-593.

42

Ibid.

The following account begins with events that occurred in the US regarding foreign currency standards. The FASB was one of the first standard-setting bodies to issue a standard on foreign currency accounting and consequently had an influence on the developments in other countries. The issuance of FAS 8, for example, created controversy not only in the US but also elsewhere. However, as the account indicates, the FASB did not operate in isolation as standard-setting bodies and MNCs from other countries also participated in the process in the US.

SEC involvement in foreign currency standards. The US standard-setting body was under the watch of the SEC in the development of standards for foreign currency but the involvement by the SEC in developing foreign currency standards was rather minimal. The FASB was formed in the same year that the Bretton Woods agreement collapsed and exchange rates went to a floating system. The FASB replaced the APB at a time when there was little confidence in the APB so not only was the FASB saddled with the task of developing a process for developing standards in general and establishing its own credibility, it came under pressure to deal quickly with the foreign currency issue. To some, this pressure was unfortunate, as it adversely affected the due process of standard-setting in the US. One controller wrote in a comment letter to the first ED on foreign currency translation:

> The Financial Accounting Standards Board was established primarily because the Accounting Principles Board had lost the confidence of the government, business community, and the profession. Part of the reasons for the loss of confidence turned on the way in which accounting principles were determined. The rules of procedure established by the FASB are an effective tool for re-establishing this confidence. These rules, however, will result in some delay in the issuance of opinions because of the thoroughness of the procedure. Recently the chief

accountant of the Securities and Exchange Commission has served notice that he will issue pronouncements if the FASB does not. Now, suddenly, the FASB has determined that 'an emergency' exists and that no public hearing and no public discussion will be held....It should not allow itself to be stampeded by Mr. Burton or anyone else.[43]

The FASB issued FAS 1, which prescribed disclosure policies only, with the stipulation that a more thorough standard would be forthcoming after more research. The pressure was on to develop this standard as the following excerpt indicates: "We recognize that the Board is under considerable pressure from several quarters to reach a conclusion on this issue and that delay produces the risk of your standard being preempted by government regulations."[44] The SEC's official position on accounting standard-setting is that it has the power to set standards but has delegated that power to other bodies, first to the Committee for Accounting Principles (CAP), then the APB, and now the FASB. It has played the part of the overseer, retaining the right to reject or pre-empt regulations drafted by the FASB. Although the SEC may have pressured the FASB to move quickly, there is little evidence that any government agency played a direct role in the choices made by the standard-setting body.

The response by the FASB to threats from the SEC can be interpreted in one of two ways. On the one hand, the FASB hastily developed and issued FAS 1 to appease the SEC. But FAS 1 lacked guidance on the major issues of translation methods and treatment of gains and losses that it really did nothing to resolve the issues. This suggests

---

[43] Letter to the FASB from DeSoto, Inc., October 24, 1973.

[44] Letter to FASB from R. J. Reynolds Industries, Inc., April 29, 1975.

that FAS 1 was merely a first step towards a standard but not a resolution by any means and that, in effect, the FASB did not succumb to the pressure to issue a standard. The Board's view was that more time was required and indeed two years passed before FAS 8 was issued. The FASB was caught between establishing credibility and showing that it would not be pushed around by government interests, whatever those would be.

The beginning of corporate pressure in developing foreign currency standards in the US. This attitude of independence and autonomy was apparent in the development of FAS 8. During the time that FAS 8 was developing, there was debate between the FASB and large corporations concerning the smoothing of earnings. In 1974 a public hearing was held concerning the topic of accounting for contingencies. The practices of corporate management at the time reflected the desire to "smooth" earnings through various accounting techniques. These practices developed as a response to the cries from Wall Street analysts who desired stable and predictable earnings. Unbeknownst to corporate managers, the FASB was opposed to income-smoothing techniques and advocated that financial statements should reflect any and all fluctuations in earnings, a position held by Don Kirk who headed the task force on foreign currency. At the public hearing in 1974, companies made clear their desire to continue the practices of accruals and other techniques that permitted the smoothing of earnings. Nevertheless, the FASB issued FAS 5 on contingencies early in 1975 requiring stringent conditions to be met before accruals can be reported, in effect eliminating a tool that corporate management had been using to smooth earnings. When FAS 8 was issued later that year, the controversy became even more heated as now the FASB instead of merely eliminating a

tool for smoothing earnings, actually created the conditions for more volatility in earnings by requiring immediate recognition treatment for the translation of gains and losses. In 1976 when the standard went into effect, the Board received numerous requests from international companies to reconsider the standard but chose not to do so.[45] These actions reflect resistance on the part of the FASB to succumb to corporate pressure.

A change in attitude. The attitude of the FASB changed two years later as the Board began to pay attention to corporate concerns. In 1978 the Board issued a call for public comment on the efficacy of the FASB standards that had been in effect for at least two years. Eighty-eight percent of the more than 200 respondents expressed concerns with FAS 8. Don Kirk was now the Chairperson of the FASB. In spite of his preference for FAS 8, the Board decided in 1979 to reconsider the standard.[46] What occurred then was indeed a reversal of action on the part of the Board. This attempt suggests an action designed to establish the FASB as a legitimate authority on accounting standards.[47] These actions coincided with the FASB's decision to involve other countries in

---

45

Van Riper, *ibid.*

46

Ibid.

47

Prior to the establishment of the FASB, the accounting profession was the authority on accounting principles. The FASB's two predecessors, the Committee on Accounting Principles and the Accounting Principles Board, were composed of members of the American Institute of Certified Public Accountants. The FASB is an independent group, not affiliated with the Institute, although some Board members are certified public accountants.

developing a new standard. It was in 1979 that the new task force on foreign currency began to invite certain interested individuals to attend the public meetings and serve on the task force, first from Canada and later from the UK and the IASC.

But standard-setters from other countries were not the only ones involved in the public deliberations. At the public meeting of the FASB task force on December 18, 1979, the representative of the DuPont corporation stated opposition to the current rate method in as much as DuPont did not agree with translating inventory at closing rates.[48] DuPont was famous for its development of the return on equity performance measurement. That measurement requires that the basis for valuing fixed assets not be changed which would happen under the current rate method.[49] Because of these concerns, DuPont led the advocates of the temporal method.[50] The Household Finance Corporation argued for reserve treatment of unrealized translation differences. The task force was not in favour of deferral because it violated the concept of recording gains and losses in the time periods in which they occurred. The Royal Dutch Shell (Shell) corporation argued against immediate recognition on the grounds that it created severe distortions in earnings and advocated the current rate method with reporting exchange differences in the balance sheet instead of the income statement. Shell also warned the

---

48
Minutes of the FASB Task Force on Foreign Currency Translation, December 18, 1979.

49
Wojciechowski, *ibid.*

50
Interview with Allan Cook, member of UK Accounting Standards Board, May 13, 1996, conducted by the author.

task force that threats from government agencies existed outside of the US and that if standard-setting bodies did not resolve the issue, the UN or the OECD or the European Economic Committee (EEC) would.[51] In reviewing the results of the Task Force meeting by the Board, the Board members were still divided on the choice of translation method, although a majority were in favour of the current rate method. The treatment of gains and losses remained an unresolved issue because Board members and those attending the meeting were divided on different treatments.[52]

Besides expressing opinions at public meetings of the task force, involvement by the MNCs occurred in the form of membership on the task force itself. In the case of the FASB, task force members are appointed by the Board to the task force. They are considered to be individuals with expertise in the area of consideration.[53] For example, the original task force which developed FAS 1 numbered fourteen members: 3 representatives of public accounting firms, 3 academicians, 1 from Morgan Guaranty Trust Co. (heavily involved in international stock broking), 1 from Merrill Lynch (an investment analyst company), Mr. Lorensen and Mr. Parkinson (who wrote theoretical articles on foreign currency accounting), 1 consultant, and 3 corporations (Mobil Oil

---

51
Minutes of the FASB Task Force on Foreign Currency Translation, December 18, 1979.

52
Minutes of FASB meeting, December 19, 1979.

53
FASB News Release, "Financial Accounting Standards Board Places 7 Subjects on Initial Agenda" (Stamford, CT: FASB, April 5, 1973).

Corp., Ford Motor Co., and Union Carbide Corp.).[54]

Another route by which corporations interacted with the FASB was via the Business Roundtable. The Business Roundtable was formed in 1972 to serve as a lobbying force for the largest US corporations in Washington. It is made up of the executives of the 200 largest US companies from the list of the *Fortune* 500. In 1976 the Roundtable became interested in accounting matters and Thomas Murphy, CEO of General Motors and founding trustee of the Financial Accounting Foundation which oversees the FASB, initiated the formation of the Accounting Principles Task Force (APTF) within the Roundtable and was its first chairperson. Ten members of the Roundtable serve on the APTF, typically executives that "have the highest level of discomfort with the financial reporting constraints imposed by" the FASB's generally accepted accounting principles.[55] In 1978, the year that the FASB decided to reconsider FAS 8, the APTF met with the FASB to discuss matters of concern, including FAS 8. Because the FASB had gone sunshine earlier that year, the meeting was publicly held, but it was the last time that the APTF would agree to meet publicly with the FASB. From then until 1982 there were no meetings but a series of letters between Mr. Murphy and Mr. Kirk. Meetings resumed after Mr. Murphy retired from General Motors and Roger Smith took over. These meetings were held in private and Mr. Smith expressed on a

---

54

FASB News Release, "FASB Task Forces Appointed for Foreign Currency Translation, Reporting by Diversified Companies" (Stamford, CT: FASB, May 31, 1973).

55

Van Riper, *ibid.*

number of occasions his disappointment concerning the standard-setting process.[56]

In developing FAS 52, a number of corporate executives were appointed by the Board to serve on the task force, including Mr. Conlyn Noland of DuPont and Mr. Ian McCutcheon of Royal Dutch Shell.[57] There are those who consider FAS 52 the "Royal Dutch" approach to foreign currency translation, because they were "the big proponents of it".[58] The reason for Shell's perspective on foreign currency accounting might be explained thus:

> Under Statement 8 you used a US dollar for a parent company currency perspective and under 52 you use a multicurrency perspective. I think for virtually all American companies, the US dollar perspective is the right one, because their shareholders are predominately American, in some cases completely--or virtually completely--American, who are interested in the ultimate cash flow in dollars. A Royal Dutch or a Unilever...They're perhaps virtually unique enterprises in that they have no nationality. Their operations and their shareholders are worldwide and maybe the multiple perspective makes sense for them.[59]

The management style at Shell may be largely responsible for their position because they viewed their foreign operations as largely autonomous, conducting business in the local

---

56 *Ibid.*

57 Interview with Conlyn Noland, assistant comptroller of DuPont Corporation, conducted by Tony Lowe, November 26, 1986.

58 Interview with Gerald White, of Grace and White, investment counsellors, November 3, 1986, conducted by Tony Lowe.

59 *Ibid.*

currency.[60] The nature of the operations also determined a company's position. Household Finance, for example, had a large loan portfolio in Canada. While the Canadian dollar fluctuated against the US dollar, companies like Household Finance suffered from volatile earnings. That would explain why they would endorse the reserve method of accounting for gains and losses to take them straight to equity and avoid the effects on the income statement.

Observations. Clearly there was opportunity for the formation of alliances between the FASB and outsiders. Coupled with the pressure to harmonize, which the FASB to a greater or lesser extent paid attention to, were the expressed opinions by specific MNCs as to the preferred translation methods and treatments for gains and losses. What remains, however, is to show how the outsiders influenced the choices made by the FASB and how the interests of the FASB came to be aligned with those of the most persuasive of the outside parties (consistent with the one-dimensional view of power). As suggested earlier, the role of government agencies in the debate was rather minimal. In the interview material and the account by Van Riper, a FASB staff member, there was little or no mention of SEC involvement in the development of either FAS 8 or FAS 52, except for the pressure to develop a standard quickly under threat of the SEC beating them to it. Academic influence was not great, at least after FAS 8 came under fire. Academic influence was minimal, as it has been with other standards.[61] The most

---

[60] Interview with Conlyn Noland, *ibid.*

[61] Van Riper, *ibid.*

influential group was international corporations. US MNC influence was predominate in developing the standards, particularly FAS 52. Had US companies been influential in developing FAS 8, the preference for smoothing earnings might have prevailed, although one cannot know for sure what would have happened if circumstances had been different. Nevertheless, it is clear that the FASB did nothing to reconsider their stance on FAS 8 until the APTF, composed of the largest US corporations with the biggest grievances towards accounting standards, became involved in discussions on accounting standard-setting. Suddenly the FASB was concerned to change FAS 8 and issue a new standard.

Because of the criticism of FAS 8, the FASB was ready to endorse the current rate method totally, in every circumstance.[62] This endorsement would have agreed partly with the UK position. The ASC endorsed both the current rate method and the temporal method, but the temporal method only in certain circumstances and mainly to accommodate US-based companies like DuPont. The preference of UK companies had always been for the current rate method. By the late 1970s Australia and Canada, in following the US lead, were endorsing the temporal method.

However, some US companies were not in favour:

> I was very closely involved with the FASB as it developed Statement 52. Their initial task was to go strictly to the current rate method. We, and a number of other companies, were able to convince them that, because of the nature of our operations, this would not have been a feasible way for us to view our business results or to manage our business. I think we were instrumental in helping them

---

[62] Interview with Conlyn Noland, *ibid.*

to develop the flexibility that is inherent in the functional currency concept,..[63]

Unlike Shell's multicurrency approach, DuPont was oriented towards the US dollar perspective because of extensive operations in the hyperinflationary economies in South America:

> I guess really it was our experience in the hyper-inflation area economies which had driven us towards a US dollar outlook in the first place because historically our international operations had been more focussed on South America than they had on Europe. I guess this was sort of a result of, in the earlier year, the cartel relationship that existed between ICI and DuPont,...we had been operating in South America for 50 years. And, of course, many of the economies there have been hyper-inflation economies. And, in that kind of system, you need some type of different measuring stick....You need some kind of standard unit of measurement. And, by and large, the dollar had provided that standard unit of measurement.[64]

There was another factor that contributed to DuPont's interest in foreign currency standards. In addition to the effect of the current rate method on management performance measures such as return on investment (ROI), DuPont was concerned about the effects of the current rate method on shareholder equity. The management at DuPont believed that the current rate method resulted in translation adjustments to shareholder equity that were not likely under the temporal method. From 1964-1978, DuPont's ROI declined steadily and prospects for expansion in the late 1970s were not good. The conditions during this time period were not good for seeking outside investment from the capital markets. Therefore, DuPont was against any accounting rules that would erode

---

63 *Ibid.*

64 *Ibid.*

their retained earnings and force them to incur higher long-term debts, which is what the corporation consequently did[65]. Eventually DuPont and other companies were able to persuade the FASB to change their position on the current rate method for all economies:

> Conlyn Noland: Originally the FASB, in developing Statement 52, had...proposed that the local currency be designated as the functional currency worldwide. That is to say that we would use current rate translation. It would be mandated worldwide including the hyper-inflationary economies....They had not thought it through. We beat on them and beat on them for a long time. I think it demonstrates the underlying balance, which to me is the underlying conceptual fallacy, in current rate translation. It just doesn't work in a hyper-inflationary economy."
>
> Interviewer: That must have been an interesting debate.
>
> Conlyn Noland: It was. It was a heated debate....Eventually they compromised with us, but it was a long hard struggle.[66]

Clearly there was resistance on the part of the FASB or the discussion would not have been so heated nor would the process have taken as much time to resolve as it did. The resistance by DuPont and other corporations also contributed to the final provisions of FAS 52, demonstrating how resistance contributed to the refabrication of the standard. It was not until 1981 that FAS 52 was finally approved. Through the arguments pertaining to the specific circumstances or management styles, both DuPont and Shell were able to persuade the FASB to prescribe the current rate method for independent operations and the temporal method for hyperinflationary economies. The current rate method became the preferred method after Shell and other MNCs exerted their pressure but not without

---

[65] Wojciechowski, *ibid.*

[66] *Ibid.*

counter-persuasion by other companies, such as DuPont who favoured the temporal method.

The situation in the UK. Involvement by a few MNCs in developing foreign currency standards was also apparent in the UK. Individuals and representatives of outside parties had opportunities to serve on the working parties on foreign currency translation. Early in the process of developing a standard for foreign currency, the deputy-treasurer of the ICI corporation, Mr. B. D. C. Ogle, was asked to prepare a paper on the "cover concept" (the matching of assets and liabilities held in the same country or currency).[67] Later Mr. Ogle was named as chairperson of a panel to prepare a draft for exposure (ED 21), based on the current rate method with provisions for offsetting gains and losses.[68] Mr. Ogle also headed the committee to review the responses to ED 21, along with three other people: Mr. N. Berman, Ms. M. E. G. Graham (deputy chief accountant of the Unilever corporation), and Mr. H. P. Gold (from Shell). Ms. Graham and Mr. Gold asked to be on the committee, while Mr. Ogle and Mr. Berman were appointed by the Committee.[69] ED 21 was not favourably received by respondents so the ASSC decided to revise it after discussing the matter further with representatives of major corporations.[70] A few months later Mr. Ogle reported to the ASSC the results of a

---

[67] Minutes of ASSC meeting, April 26, 1975.

[68] Minutes of ASSC meeting, February 23, 1977.

[69] Minutes of ASSC meeting, April 26, 1978.

[70] Minutes of ASSC meeting, June 12, 1979. The names of the corporations were not

meeting with finance directors in which they supported the net investment concept with a provision for offsetting exchange differences on loans against the foreign investment.[71] ED 27 was approved for publication the next year, October, 1980. Finance directors again met with the working panel in January, 1981.[72] Mr. Ogle was again chairperson of the panel that reviewed the comments on ED 27.

Some government involvement in the UK. Late in 1981, the Department of Trade (DoT) in the UK raised some issues concerning treating translation gains and losses as realized.[73] The ASSC later met with the DoT,[74] resulting in a decision to distinguish between exchange gains on short-term monetary items and those on long-term monetary items. The gains from short-term items are to be reported in the profit and loss statement in accordance with Schedule 8 of the Companies Act 1948, but to report the long-term unrealized gains as such would be an exception to the Companies Act. Five of the Councils of the CCAB approved the draft for SSAP 20 on those terms.[75]

One Council objected, on behalf of the British Bankers Association, to regarding

---

recorded in the minutes.

71 Minutes of ASSC meeting, September 14, 1979. Names of individuals or the companies they represented were not recorded in the minutes.

72 Minutes of ASSC meeting, February 25, 1981.

73 Minutes of ASSC meeting, December, 16, 1981.

74 Minutes of ASSC meeting, February, 24, 1982.

75 Minutes of ASSC meeting, September 29, 1982.

only exchange gains on settled monetary items or those to be settled within one year as realized and reported on the profit and loss statement.[76] Gains and losses on long-term monetary items are considered unrealized, according to Schedule 8 which requires that only realized gains and losses be reported on the profit and loss statement.[77] Banks are exempt from Schedule 8,[78] implying that banks can report gains and losses on long-term monetary items on the current year's profit and loss statement. Apparently the banks' objections had an effect because the following month, SSAP 20 was changed to require reporting exchange gains and losses on both short-term and long-term monetary items "in accordance with the accrual concept of accounting".[79] This is another example of how resistance contributed to the development of the standard.

Effects of MNC involvement in the UK. In the UK there was a difference of opinion on foreign currency accounting among some of the major corporations similar to the battle between Shell and DuPont in the US. In the UK two of the major players were Unilever and ICI. ICI deputy-treasurer, Mr. Ogle, was in a strategic position to influence the deliberations on foreign currency standards as head of the ASSC committee to write the first exposure draft and then to review the subsequent comments. It is not surprising

---

76 Minutes of ASSC meeting, September 29, 1982.

77 Minutes of ASSC meeting, January 26, 1983.

78 Minutes of ASSC meeting, December 22, 1982.

79 Minutes of ASSC meeting, January 26, 1983.

then that ED 21 followed the ICI approach to foreign currency accounting.[80] While developing ED 27 and SSAP 20 ICI influenced deliberations later on in relation to the offsetting provisions. The ASC always had an expressed interest in harmonization, but UK companies objected to the restrictive provisions concerning hedging. In the US the rules required that companies notify auditors in advance of a hedging transaction and that offsetting loans and assets be in the same currency. ICI was one of the UK companies opposed to those provisions as the company had huge borrowings but no foreign assets in Swiss francs. Consequently, the company would suffer from huge losses on those borrowings on the profit and loss statement as per ICI's preferred treatment.[81] It is not clear whether there were other reasons for ICI's concern over foreign currency standards, such as those discussed for DuPont or those discussed below for Unilever and Shell. ICI, like DuPont, favoured the temporal method. These two corporations once created an alliance to allow technological information to flow between them,[82] but that agreement had been dissolved long before deliberations on foreign currency standards began, so an alliance between ICI and DuPont is not a likely explanation for ICI's interest in this matter. In the end, the ASC gave way to the pressures of ICI and permitted global offsetting; in other words, losses on borrowings could be offset by gains on assets in

---

80

Interview with Allan Cook, May 13, 1996.

81

Minutes of ASSC meeting, September 29, 1982.

82

Graham D. Taylor and Patricia E. Sudnik, *DuPont and the International Chemical Industry* (Boston: Twayne Publishers, 1984).

other currencies.[83]

Meanwhile Unilever had been working all along to make its position known. Unilever favoured the current rate method because of the unique position the company was in having two parent companies, Unilever Ltd in the UK and Unilever NV in the Netherlands, which functioned as one. The two parent companies were linked by a number of agreements including a program for dividend distribution called the dividend equalization agreement. Under that agreement, shareholders of either parent company would receive an equivalent amount of dividends whether it be in sterling or guilders.[84] As soon as exchange rates floated, Unilever became concerned, to say the least. On its own the company in 1973 developed a system that solved the problem. That system is what ultimately became FAS 52. When FAS 8 came out, Unilever quickly realized that the temporal method would yield non-equivalent dividends in their program and hence became interested in the development of foreign currency standards. ED 21 raised similar concerns due to the immediate recognition treatment for gains and losses.[85] Realizing that ED 21 wouldn't work, Unilever strategically placed Ms. Graham by requesting that she serve on the panel with Mr. Ogle, along with Mr. Gold, who was also in favour of the current rate method.

---

[83] Minutes of ASSC meeting, September 29, 1982.

[84] Christopher Tugendhat, *The Multinationals* (New York: Pelican Books, 1984); Charles Wilson, *Unilever 1945-1965: Challenge and Response in the Post-War Industrial Revolution* (London: Cassell, 1968).

[85] Minutes of ASSC meeting, September 29, 1982.

Shell was particularly interested in the outcome of the deliberations. In addition to the reasons stated earlier for Shell's interest in foreign currency standards, the ownership structure at Shell may also explain this interest. Like Unilever, Royal Dutch Shell is owned by a British company (40% by British Shell Transport and Trading) and a Dutch company (60% by Royal Dutch). Also like Unilever, Shell is interested in maintaining a balance between the shareholders in each company by dividing dividends according to their respective ownership percentages.[86] Therefore, the temporal method would have similar repercussions at Shell as it would at Unilever. In the beginning, Shell wished to endorse FAS 8, but first quarter financial results in 1978 were a disaster. Shell quickly became an advocate of the current rate method and urged the FASB towards harmonization. Shortly thereafter the FASB decided to review FAS 8 and asked Ian McCutcheon (from Royal Dutch Shell) to serve on the US task force, the first non-American to do so. Meanwhile Mr. Gold was placed on the working panel in the UK. Consequently ED 27 more closely resembled the Unilever approach.[87]

Unilever, along with Shell as an ally, was able to infiltrate the thinking of the ASC and ultimately the FASB and the IASC. Allan Cook began serving on the IASC in 1978. He came from the Unilever corporation. Also, Unilever's deputy to the controller, Charles Molligan was appointed to the IASC steering committee for foreign currency.[88]

---

[86] Tugendhat, *ibid.*

[87] Interview with Allan Cook, May 13, 1996.

[88] *Ibid.*

Mr. Gold also served on that committee so Shell was represented at the IASC as well as the FASB and the ASC. The IASC was rather cautious in developing standards on foreign currency as it wanted to wait and see what the US and the UK were going to do. The IASC did meet with Canada, at the CICA's request, and the ASC during the time that Canada was struggling to resolve the issue of gain and loss treatment. Mr. Cook began serving on the FASB task force on foreign currency in 1980. At the time he was serving as Secretary of the IASC. Prior to serving as Secretary, Mr. Cook's job was to reactivate the foreign currency issue at the IASC. In that capacity he wrote papers for the IASC and also for the ASC and the FASB.[89]

Observations. Through strategic placing of key people on task forces and working parties internationally, Unilever and Shell were able to convince the standard-setting bodies to align more closely with their preferences for foreign currency accounting. The opposition and much of the resistance to their view point came not so much from the standard-setting bodies but from other corporations equally set on persuading others to their point of view. Shell and Unilever were more interested in international harmonization than ICI or DuPont,[90] although the reasons for that interest is not evident.

The conflict in Australia. The situation in Australia was a bit more complex. The AARF, which was ultimately responsible for drafting accounting standards, was

---

[89] *Ibid.*

[90] *Ibid.*

influenced by industry, a major public accounting firm, and another standard-setting body in Australia. The other standard-setting group, known currently as the Australian Accounting Standards Board (AASB), was preceded by the ASRB, set up in 1984 for the purpose of sponsoring, reviewing, and approving accounting standards. The ASRB was preceded by the Accounting Standards Review Committee (ASRC), formed in 1976 by the Joint Standing Committee of the Australian Society of Accountants (ASA) and the Australian Institute of Chartered Accountants (AICA). These groups originated in the profession. The AARF, originally called the Accountancy Research Foundation, was formed in 1966 to conduct research in accounting because there was dissatisfaction with academic research at the time. Two committees of the AARF were involved in standard-setting for foreign currency. The first one was the Accounting and Auditing Research Committee, which developed the ED in 1973. This group was replaced in 1974 by the currently existing Australian Accounting Research Committee (AARC) which has not been directly involved in standard-setting. The other committee, now called the ASB, formed in 1981, has been the main group involved in standard-setting. Originally this committee was called the Australian Accounting Standards Committee (AASC) and was formed in 1974 for the purpose of developing accounting standards.

The relationship between the Foundation's ASB and the profession's ASRB was to be one of the ASB providing the ASRB with standards to review and approve. In the case of foreign currency accounting, there was conflict between the two groups, although initially there had been much collaboration on the pronouncements on foreign currency between the Foundation and the profession. In 1972 the Foundation, at the request of the

AICA, went to work to draft an exposure draft on foreign currency accounting. A four-member Project Advisory Committee assisted the Foundation's director of accounting research in the project. Drafts of the proposed exposure draft were sent to a joint committee of the ASA and the AICA which reviewed it and their comments were reviewed by the project director and Dr. Bruno Feller, an academic on staff with the Foundation. Once the ED was issued, a separate committee was appointed to review the comments, composed of Mr. I. Philip, from Price Waterhouse (a major international public accounting firm) and Mr. D. Rickard.[91] Interestingly, there were only 2 objections to the current rate method out of 28 responses. One of these came from Price Waterhouse and the other came from the Comalco corporation, whose chief accountant was one of the four people on the advisory committee![92]

In 1975 a review committee, consisting of Mr. Rickard, Mr. Philip (both to represent the AASC), and Mr. Malcolm Miller (from the University of New South Wales to represent the AICA), was set up to review the comments on the 1973 ED.[93] Later Dr. Feller prepared and submitted to the AASC a paper summarizing the major criticisms of the ED and the issues currently being considered by the FASB and the IASC.[94] Some

---

91
AARF Currency Translation History Sheet; Minutes of meetings: Accounting and Auditing Research Committee, February 19, 1973; Joint Accounting Principles Committee of ASA and AICA, May 10, 1973, June 12, 1973, September 13, 1973.

92
From the Summary of Comments on 1973 ED, AARF files.

93
Minutes of AASC meeting, May 30, 1975.

94
AARF Currency Translation History Sheet; Minutes of AASC meetings, August 1, 1975,

companies were not in favour of the immediate recognition treatment for gains and losses recommended by the ED and made their positions known. In a letter from the AICA to the chairperson of the AASC, accompanied by a letter to the AICA from an anonymous company, the position of six publicly-held companies that favoured a reserve treatment was emphasized. The company's letter reported the footnotes of these companies explaining the widespread use of the reserve treatment as evidence of the popularity of the treatment.[95] The letter pointed out that other member firms of the AICA were also in favour of the reserve treatment. Thus, companies pleaded their case via soliciting the help of the profession through the AICA.

In November 1977 the Joint Committee of the ASA and the AICA made an unprecedented move by commissioning a public accounting firm, Price Waterhouse, to prepare a new ED on foreign currency accounting.[96] Price Waterhouse accepted the assignment with Mr. Philip as contact person.[97] The ED was issued in June 1979, endorsing the temporal method and amortization of gains and losses on long-term monetary items and immediate recognition for short-term items. This ED amounted to an almost complete reversal of the 1973 ED, and was not in agreement with the AARF.

March 3, 1976.

95

Letter to Mr. J. D. Balmford, Chairperson of AASC, from AICA, August 23, 1976.

96

Letter to Price Waterhouse from Mr. A. W. Graham, Secretary of Joint Standing Committee, November 23, 1977.

97

Letter to Mr. Graham from Price Waterhouse, November 28, 1977.

The technical director of the AARF, Kevin Stevenson, explained to Mr. Philip what was expected of him and his firm. The Foundation's Executive Committee had considered the submissions on the 1973 ED and had determined that the next step was the development of a standard based on the current rate method. The issue of treating exchange differences was to be in accordance with predominant practice, which Price Waterhouse was to determine empirically.[98] Mr. Philip responded with a report in which he outlined the reasoning for endorsing the temporal method and reported that the practice on treatment of exchange gains and losses was quite varied, although the largest Australian companies preferred the deferral method. He also suggested a delay in issuing a standard while other countries and the IASC finished their work in view of the varied results of the survey.[99] Interestingly, it was Price Waterhouse that had collated the submissions on the 1979 ED and prepared the report which prompted the letter from Mr. Stevenson to Mr. Philip in December.[100] The Foundation did agree in April 1980 to await the results of international developments before issuing a standard.[101]

In 1982, the newly formed ASB took over the foreign currency project. A new draft was reviewed but no decisions were made until June 1983, at which time they

---

98
Letter to Mr. Philip from Kevin Stevenson, Technical Director of the AARF, December 18, 1979.

99
Report to Kevin Stevenson from Ian Philip, February 11, 1980.

100
AARF Project History on Foreign Currency Translation.

101
Ibid.

decided to endorse the deferral method for translation gains and losses on long-term monetary items and the current rate method. At that time they also agreed to invite experts on foreign currency to attend the next meeting.[102] Certain amendments were agreed to at that meeting[103] and ED 24 was issued in September, 1983. Further deliberations ensued in the preparation of a standard. Differences of opinion as to translation method continued between Mr. Stevenson who favoured the current rate method and others who favoured the temporal method.[104] Finally, in February 1985, the ASB agreed to prescribe the current rate method for self-sustaining operations and the temporal method for integrated operations.[105] According to submission letters, the immediate recognition treatment was well-supported but the Board felt that this was not a practical option in the Australian environment.[106] At that meeting the Board also decided that re-financed loans were considered settled as opposed to extended.[107] The ED specified that gains and losses on settlements were to be reported on the profit and loss statement, rather than deferred.

102
Minutes of ASB meeting, June 22 and 23, 1983.

103
Minutes of ASB meeting, August 3 and 4, 1983.

104
Minutes of ASB meeting, December 5 and 6, 1984.

105
Minutes of ASB meeting, February 13 and 14, 1985.

106
The meaning of "not a practical option" is not clarified in the minutes (see next footnote).

107
Minutes of ASB meeting, March 13 and 14, 1985.

When the ED was issued in October 1985, it brought a howl of protests from the mining industry. The representatives of the mining companies objected to the settlement status of a re-negotiated loan, insisted instead that the resulting gains and losses be deferred as all other unrealized gains and losses on long-term monetary items.[108] A special meeting was held between the ASB and nine industry representatives in November.[109] Mr. Stevenson was adamantly against buckling to the pressure of a single industry and in the end the Board determined that a convincing case for change had not been made.[110] One of the arguments made by the ASB was that the proposed practice by the mining companies was inconsistent with international practices endorsed by the US, the UK, and Canada.[111]

Conflict began to occur between the AARF and the ASRB, shortly after the latter was formed. In September 1985 the ASRB released ASRB 1003, *Foreign Currency Translation--Disclosure*, which specified the disclosures required concerning foreign

---

108

Letter to Chairperson of ASB from CSR Limited, October 17, 1985. Also testimony by the assistant General Manager of Finance of CSR to ASB meeting on August 28 and 29, 1985. Also letters and telexes from Western Mining Corp., Ltd., Woodside Petroleum Ltd., Mount Isa Mines Ltd., CRA Ltd, and Australian Mining Industry Council Elders IXL Ltd., among others (13 in all) received during the month of October concerning the definition of settlement (Minutes of ASB meeting, October 23 and 24, 1985).

109

Memo from J. N. Miles, Chairperson of ASB, to Chairperson of AARF, December 5, 1985.

110

Based on interviews by Jim Paul in an unpublished history of the AARF by Jim Paul, staff member of AARF, and minutes of ASB meeting, December 3 and 4, 1985.

111

Article in Business Review Weekly, "Miner Fail in Forex Write-off Bid", December 20, 1985.

currency. Results of the November meeting with mining representatives and all other materials and information concerning the review of the October ED were sent to the ASRB.[112] In March 1987, long after AAS 20 had been released, the ASRB took the view that a standard on foreign currency accounting should require immediate recognition of gains and losses on long-term monetary items. The ASB decided to canvass the Foundation's mailing list for comments on the issue of deferral versus immediate recognition.[113] Shortly thereafter, the ASRB informed the ASB that they were in unanimous agreement to require immediate recognition for several reasons, one of which was harmonization with the US and the UK.[114] However, the results of the ASB poll showed that the majority of respondents strongly disagreed with the ASRB proposal for immediate recognition.[115] The ASB decided to submit to the ASRB a working document outlining the ramifications of immediate recognition.[116] The Board was evenly divided between immediate recognition and deferral, but in view of the ASRB's decision to require immediate recognition, the ASB resolved to change AAS 20 to require immediate

---

112 Memo from J. N. Miles, Chairperson of ASB, to Chairperson of AARF, December 5, 1985.

113 Minutes of ASB meeting, March 3, 1987.

114 Letter to J. N. Miles, Chairperson of ASB, from S. J. Droder, Chairperson of ASRB, March 20, 1987.

115 Memo to ASB from Jim Paul, Project Manager for Foreign Currency, May 8, 1987.

116 Minutes of ASB meeting, May 5, 1987.

recognition.[117] Perhaps the decision to change AAS 20 reflects the true "interest" that the Foundation had in the issue, but the initial resistance depicted another concern. Warren McGregor stated that the Foundation

> saw the foreign exchange reversal as a watershed in the development of the ASRB. That single action effectively signalled the demise of our own standard-setting board and established the ASRB as the standard setter for Australian companies. Privately, [Foundation] staff were glad about the foreign exchange standard. We had always believed in immediate recognition.[118]

So the ASB acquiesced on the grounds of agreement with the principle of immediate recognition but resisted by trying to solicit the views of outside parties as to its detriments. The real issue, perhaps the real interest, of the ASB at this point in time was its own legitimacy as a standard-setting body. Ultimately, however, the standards that were adopted by the ASB closely resembled those of the US and the UK. Indirectly, the MNCs involved in the development of foreign currency standards in those countries also affected the resulting standards in Australia because of the interest and pressure to harmonize with those other countries.

Canadian situation less clear. Information concerning the developments of foreign currency standards in Canada is rather scant, for reasons explained earlier. In a letter to Dr. Bruno Feller, Technical Director of the AARF, David J. Moore, the Senior Research Manager on foreign currency at the CICA, indicated that the life insurance

---

117 Minutes of ASB meeting, June 24, 1987.

118 Interview with Warren McGregor by Mr. Burrows of the AARF staff, January 17, 1995, quoted in the unpublished history of the AARF by Jim Paul, staff member of the AARF.

industry and the real estate industry were concerned with certain provisions of the Canadian ED.[119] These industries were likely in favour of the deferral method, according to the letter. Details of the detriment of immediate recognition were not apparent in the letter and specific companies were not named. However, like the AARF, the CICA ultimately developed foreign currency standards comparable to those of the US and the UK.

Overall observations. The evidence presented here describes the influence of a few MNCs in the process of developing foreign currency standards. While other entities did exert their opinions, the final outcomes were based on the expressed preferences of those MNCs in a position of power to influence the process. The evidence raises questions regarding why would certain MNCs become involved in the process and not others. The account indicates why Shell, Unilever, DuPont, ICI, etc., became interested in the outcomes of the deliberations, but it does not explain why other MNCs did not participate in the process. Perhaps the unique situations of these particular MNCs (which may not reflect overall multinational corporate activity) were affected more by certain provisions of these standards than others. In that case, it certainly was not the majority point of view that won out over the preferences of a few unique situations. This question remains unresolved and would require further study.

The development of foreign currency standards occurred in the midst of larger social and economic developments. The events and circumstances of the time period

---

[119] Letter by David J. Moore, CICA Senior Research Manager on foreign currency, to Dr. Bruno Feller, Technical Director, AARF, dated June 13, 1979.

have already been discussed in this dissertation. However, the influence of certain discourses prevalent at the time, specifically international harmonization, also affected the processes involved in this development. As the push for harmonization was lobbied for, these effects determined the course of developing foreign currency standards in a larger context in terms of who would benefit from these standards and whose voices would be heard during their development. While overt conflict is relatively easy to observe in this process, the latent conflict suggested by Lukes' three-dimensional view must also be considered to fully understand the wider social effects of accounting in general which ultimately influences the development of specific standards. The following section illustrates how the interest in international accounting harmonization developed and played a role in developing foreign currency standards.

III. Efforts to Harmonize Standards on Foreign Currency Accounting

Preston, *et al,* provides a useful procedure for examining the construction of a technology and the processes involved in its fabrication. These procedures are based on Latour's notion of studying science in action to uncover the ways in which interests become interests and how ideologies are translated into technologies. As stated earlier in this chapter, it is important in this study to establish that it was in the expressed interest of parties involved to harmonize accounting standards for foreign currency accounting. It is not enough merely to establish that the interest was there but also how it developed. The purpose of this exercise is to demonstrate the role of discourse in the outcomes of

accounting regulation.

The first step taken by Preston, *et al,* was to examine government documents for the use of rhetoric to frame issues and silence sceptics. Latour discusses four tactics in dealing with uncertainty and opposition.[120] One of these is fortification in which the text is ladled with increasingly technical material and appeals to other "accepted truths" so as to make it harder to for the opponent to beat it.[121] Stacking involves persuading the reader by bringing into the text figures and numbers and gradually making generalizations from these detailed figures. Staging and framing involves presenting statements in such a way as to aim at the ideal reader and anticipate the reader's objections. The fourth tactic is captation in which the reader's objections are controlled by offering statements that are difficult to object to and moving to more contestable statements, making it logically more difficult to object to the latter.[122] To a greater or lesser degree, these tactics were found in the text of documents relating to management budgeting in hospitals in Preston, *et al.*

This section first examines the rhetoric on the international harmonization of accounting practices. The rhetoric on harmonization was prevalent in the popular press during the time period under study. The purpose of this exercise is to suggest that the interest in harmonization was discursively formed and had its basis in the political and

---

120
Latour, *ibid.*

121
From Preston, *et al, ibid.*

122
Latour, *ibid.*

economic conditions of the late 1960s and early 1970s, which was also when the IASC and some of the other standard-setting bodies in the countries under study were formed. The documents examined for this part of the study mainly include articles written in the popular press by accountants, academics, and corporate managers. The discussion begins with evidence concerning an interest in harmonizing foreign currency standards.

The Harmonization of Standards for Foreign Currency Accounting

The development of standards for foreign currency accounting began in the midst of determining the purpose of financial reporting and the movement toward harmonization. Although the discourse on harmonization was quite prevalent at the time, the task of harmonizing standards was difficult. Much of the controversy over foreign currency accounting began with the issuance of FAS 8 by the FASB in 1975. The UK and Australia favoured the current rate method over the temporal method endorsed in FAS 8, and Canada favoured the deferral treatment of translation gains and losses over the immediate recognition treatment of FAS 8. At the time, the FASB did not appear concerned to achieve international harmonization in developing standards for foreign currency. In the early stages of drafting exposure drafts in the US, references were made concerning the positions of the Institute of Chartered Accountants of Scotland, Parkinson's CICA study, and the Australian ED issued in 1973,[123] but there was no mention of trying to harmonize with other entities. Reference was made in the same document concerning the use of the current rate method in other countries, but noting

---

123 FASB, *ibid.*, February 21, 1974.

that it was not an acceptable method in the US.[124]

Nevertheless, harmonization was on the minds of some individuals. In a public hearing held on June 10-11, 1974, Don Kirk, who headed the FASB task force on foreign currency, asked the US representative to the IASC, Joseph Cummings, about the international scene:

> Mr. Kirk: I would love to ask you a question about what might happen on the international scene on translation but....
>
> Mr. Cummings: Well, this is an opportunity around the world for a number of groups to do this job simultaneously. I am hopeful that we will have an opportunity to work with your group as your ideas are firmed up and perhaps solve the problem in the same way. That's my hope, but it means we will all have to listen a little bit.[125]

In spite of the wishes of the IASC to work together with the FASB, the group at Stamford, CT, seemed to operate without considering other groups until FAS 8 came under fire in the late 1970s. In 1979, the task force on foreign currency accounting held a series of public meetings. It is not known what, if any, groups or individuals participated in, or observed, the FASB meetings in the development of FAS 8,[126] but beginning in 1979, members of other standard-setting bodies were invited to become

---

124 *Ibid.*

125 *Public Record Discussion Memorandum on Accounting for Foreign Currency Translation--dated February 21, 1974* (Stamford, CT: FASB, 1974), p. 73. (The Discussion Memorandum was published in February, 1974. This document discusses that memorandum and was published later that year.)

126 The FASB did not go "sunshine" until January, 1978. Records of meetings of the FASB and the foreign currency task force are not available prior to that time.

members of the task force. At the first meeting held in March and at the second meeting held in May, representatives from the CICA attended as observers.[127] In December, the proceedings of the meeting included reports from the UK and Canadian projects. The representatives of each of these countries reported on the current status of their respective projects and also expressed an interest in the results of the FASB deliberations. James Carty, the Secretary of the ASC, reported, "With the second of two exposure drafts concerning foreign currency translation still outstanding, the UK Institute awaits with interest the outcome of the FASB's deliberations."[128] David Moore of the CICA expressed similar sentiments and stated also an interest in international harmonization:

> After learning of the FASB's Statement No. 8 Reconsideration project, the CICA decided to rescind a pronouncement of its own.....Like its UK counterpart--and in the interest of achieving international harmony in practice--the CICA awaits with interest the results of the FASB Reconsideration project.[129]

At this point there was on the part of these standard-setting bodies an expressed interest in the FASB activities and also a desire to resolve the issue. As James Carty reported,

> The UK places high priority upon resolving the foreign currency translation issue due to the significance of foreign trade to its economy and to the impacts of severe inflation coupled with a weakening currency, particularly against those of

---

127 Gertrude Mulcahy in March and David Moore in May, from the minutes of task force meetings, dated March 30, 1979 and May 1, 1979, respectively.

128 Minutes of task force meeting held on December 18, 1979, Stamford, CT.

129 *Ibid.*

the other EEC countries.[130]

These statements by Mr. Carty and Mr. Moore suggest that harmonizing foreign currency standards was indeed in the interest of the parties involved. The FASB's statement in FAS 52 implies an interest in international harmonization also:

> The Board also believes that, to the extent practicable, the accounting for the translation of foreign currency transactions and financial statements in the United Sates should harmonise with related accounting practices followed in other countries of the world. The Board maintained close liaison with representatives of the International Accounting Standards Committee and the accounting standards-setting bodies in Canada and the United Kingdom and Ireland as this Statement was developed. Representatives from each of those groups were active participants with the Board's foreign currency task force.[131]

The next meeting of the task force was held in April of 1980. The ASC and the CICA sent the same representatives and this time the IASC was represented. Allan Cook, Secretary of the IASC, was appointed as a member of the task force at that time.[132] At a task force meeting in June, 1981, the IASC, the CICA, and ASC reported updates. At that point, the IASC had issued a discussion draft of a foreign currency proposal and was awaiting responses from 50 countries. The CICA and ASC were both on the verge of issuing new exposure drafts but were interested in the outcome of the US deliberations. David Moore reported, "...the CICA continues to await the outcome of the

---

130 *Ibid.*

131 FAS 52, para. 76.

132 Minutes of task force meeting held on April 24, 1980, Stamford, CT.

FASB's foreign currency translation project before issuing its own standard."[133] However, he went on to describe the differences that still existed between the US and Canadian approaches, which were mainly concerning the treatment of gains and losses. The ASC had analysed comment letters on ED 27 and James Carty reported that most of the comments were in support of the ED, so there was not likely to be any changes to the ED. Nevertheless, the ASC was not going to issue a standard until the US project was finished; "...the ICAEW will await the outcome of the FASB foreign currency translation project before issuing a final standard."[134]

Thus, the IASC, the CICA, and the ASC kept close watch of the FASB activities while working on their own standards, even to the extent of not issuing new standards until the outcome of the FASB's work on revising FAS 8 was known. Did these other groups await the outcome of FASB decisions to see if the US would align with their own standards or was it that they intended to align their standards to FAS 52 once the US settled on what they would do? Or was this an opportunity to try to influence the FASB to align the US interests with those of Canada or the UK or the IASC? For what purpose did the FASB invite the other countries to participate on the task force in the first place? The FASB wished to be informed on developments in other countries but does this imply an interest in harmonization? Although FAS 52 was more closely aligned with Canadian and UK standards, differences still existed. Was it really in the interests of standard-

---

133 Minutes of task force meeting held on June 4, 1981, Stamford, CT.

134 *Ibid.*

setters to harmonize internationally or merely to learn from the mistakes of the FASB? Was it in the interests of standard-setting bodies to harmonize accounting standards for the purposes of protecting investor interests? Was there pressure from capital markets to do something to ensure that investors would have access to information that was comparable so that markets could not be distinguished by the amount or quality of information disclosed by companies listing on their securities exchanges? Would the capital markets even want to eliminate the competitive edge that different levels of information might offer to them?

A closer look at the attitudes of the standard-setting bodies may reveal some answers. The FASB has not played a major role in efforts to harmonize accounting standards internationally. The support of the FASB has been there but Don Kirk's conviction, while he was chairperson of the FASB from 1978 until 1987, was that the FASB was in a special position under the oversight of the SEC and therefore must devote its resources exclusively to financial reporting for US companies within US borders, while at the same time cooperating with international bodies. Dennis Beresford, who succeeded Kirk in 1987, recognized increased pressures for international harmonization but would not commit the FASB to participate in the effort.[135] In reference to an appearance by a board member at an OECD conference in Paris, an executive of a large US corporation recalled that the board member stated that the FASB was very little influenced by or very little inclined to expend resources in cooperating with the IASC

135

Van Riper, *ibid.* Van Riper is a former staff member of the FASB who served from 1973-1991.

and were not concerned much by the development of international standards.[136] International harmonization was not a priority for the FASB as it might have been for other standard-setting bodies.

The ASC (then known as the ASSC) in the UK first began to express an intent to cooperate with other standard-setting bodies in developing foreign currency standards in 1979. After discussions held with the CICA and the FASB in 1979, the ASC decided to cooperate more closely with both bodies.[137] James Carty was very much in favour of harmonization:

> Significant developments are taking place in North America and ASC is also following the progress made in the review of the standards set in other countries in the hope that it may be possible to bring about a greater degree of harmonization between the standards produced by different national bodies than has been found possible in the past.[138]

In December, as noted, James Carty attended a public meeting of the FASB task force. At this time, the ASC was also monitoring the developments in Australia, where an ED had been released in June. By early 1980, after a meeting of an ASC staff member with the CICA and the FASB, the ASC believed that the FASB was moving closer to the position of UK.[139] A few months later (October, 1980), the ASC approved ED 27 for

---

136 Interview with Conlyn Noland, *ibid.*

137 Minutes of ASSC meeting, September 9, 1979.

138 Letter written by James Carty in preparation for a meeting with the IASC on November 14, dated November 2, 1979.

139 Minutes of ASSC meeting, February 2, 1980.

publication. Things were beginning to look optimistically towards more harmony in foreign currency standards internationally. In the preface of an earlier draft of ED 27, the ASC stated,

> A number of meetings have been held between members of ASC, the FASB and the Canadian Institute to exchange views on developments in each country and to explore ways in which a degree of harmonisation could be achieved in the revised standards which will be published in each country. It is now clear that the ASC and the FASB have reached very similar conclusions as a result of the reviews of their own positions.[140]

In the interest of international harmonization, the ASC later decided in SSAP 20 to permit the average rate in translating profit and loss statements since FAS 52 requires the average rate.[141] Clearly, the UK body was interested in harmony but, as will be indicated in the next section, the release of ED 27 raised a number of issues by outside parties which may have hampered the resolution of differences in foreign currency standards. A number of UK companies objected to FAS 52 which caused a delay in issuing SSAP 20.[142] Also, not all interested parties were keen on harmonization in the UK, at least in the early days. Sir Ronald Leach, who was Chairperson if the ASSC, in his address to the AASC in 1974, referred to his belief that international standards will lay unnecessary burdens on local enterprises not involved internationally and to his concern over the speed with which the IASC was addressing some issues not yet addressed by the ASSC,

---

140 Preface to August 1980 draft of ED 27.

141 Wallace and Ogle, *ibid.*

142 Carty, *ibid.*,1995.

which results in the danger of international standards being issued before national standards.[143]

The Canadian position had been to look to the UK, the US, and the IASC for guidance in developing standards for foreign currency accounting. Prior to the release of the ED in 1977, the CICA reviewed FAS 8 and ED 21 in preparation for finalizing the Recommendation.[144] Many of the respondents to the 1977 ED, in disagreeing with the ED, stated that the CICA should delay any decisions concerning a final Recommendation until the US deliberations were finished and until pronouncements by the IASC and the ASC were finalized.[145] In September 1978 the Accounting Research Committee (ARC) of the CICA released Section 1650 but suspended it in February 1979 while the Committee studied the impact of 1650 and considered the international developments in foreign currency accounting, particularly in the US. As in the US, companies were objecting to the provisions of Section 1650.[146] This attitude carried forward in developing the 1982 ED:

> In the course of its deliberations, the ARC has monitored international developments and, although there are some differences, has attempted to harmonize its proposals with those of other standard setting bodies, particularly

---

143 Minutes of AASC meeting, November 11, 1974.

144 Moore, *ibid.*, 1977.

145 Moore, *ibid.*, 1978.

146 Letter by the Chairperson of the Accounting Research Committee to CICA Handbook subscribers, dated February 23, 1979, cited in *Financial Reporting in Canada,* Fourteenth Edition 1981 (Toronto: CICA, 1981).

those of the International Accounting Standards Committee (IASC) and the US Financial Accounting Standards Board (FASB).[147]

In the end, AR 1650 was issued in 1983 with a certain degree of harmony with FAS 52, SSAP 20, and IAS 21.[148] International harmonization was at the very least an expressed interest on the part of the CICA.

In Australia, the AASC monitored the international developments in foreign currency accounting, particularly the activities of the IASC. The Committee disagreed with the IASC's ED issued in September 1976 concerning the treatment of gains and losses on long-term items,[149] and relayed their objection to the IASC. In developing ED 11 in 1979, it was the belief of the AASC Technical Director that developments in other countries may influence the Australian standard:

> While the standard is being prepared it is intended to closely review developments in the US, UK and Canada. Such developments may determine the date of release, and even the ultimate contents of, the Australian standard.[150]

Mr. Philip, to whom that statement was written, responded that the AASC should delay its issue of a standard until deliberations in the US, Canada, and the UK were finalized.[151]

---

147 Preface to Exposure Draft, 1982.

148 Paul Dunne, "Foreign Currency Translation at Alcan", *CA Magazine* (October 1983): 40-49.

149 Minutes of AASC meeting, November 3, 1976.

150 Letter from K. M. Stevenson, AASC Technical Director, to Ian Philip at Price Waterhouse, December 18, 1979.

151 Letter from Ian Philip to K. M. Stevenson, February 11, 1980.

This concern was repeated in a letter from an executive of an Australian company.[152] Others, however, were more concerned with a speedy resolution to the problem and did not agree to wait on the developments of other standard-setting bodies.[153] Meanwhile, the project coordinator for the foreign currency project in the AARF, in his comments on an IASC exposure draft, mentioned: "Accounting for foreign currency translation is an area where it is particularly important to achieve international harmonisation of accounting standards."[154] The comment letter described what differences there still were between the current Australian ED and the IASC ED. ED 24, issued in 1983, was more in line with IAS 21, so a degree of harmonization was achieved. In developing AAS 20 in 1985 the ASB, as it was then called, and the Public Sector Accounting Standards Board (PSASB) were keen on achieving harmonization with other countries' standards. By that time, IAS 21, FAS 52, SSAP 20, and AR 1650 had been issued. In a letter to the AICA, the Chairpersons of those two groups stated, "An important aspect of the Statement's development has been the desire of the Boards to have maximum compatibility with the approaches adopted internationally."[155] The letter then pointed out the differences that exist in the treatment of gains and losses on monetary items, pointing

---

152
Letter from CSR Limited to K. M. Stevenson, March 20, 1980.

153
Letter from Repco Limited to K. M. Stevenson, May 1, 1980.

154
Comment letter to the IASC by David Roberts, project coordinator, AARF, October 1981.

155
Letter to Mr. Prosser, Secretary of the Joint Standing Committee of the Institute of Chartered Accountants in Australia, dated August 12, 1985.

out the Australian and Canadian preferences for deferral and the US and UK preferences for immediate recognition. So while harmonization was an expressed desire, differences in standards continued to exist (although it might be difficult to measure the significance of these differences). In 1987 the ASRB released Media Release 87/1 which asked for the AARF to resubmit AAS 20 and to change the provision for treatment of gains and losses to immediate recognition, the reasoning based on consideration of international standards, particularly those in the US and UK.[156] Eventually AAS 20 was amended to prescribe immediate recognition.

From the beginning, the IASC was urging harmonization. In a letter to the Chairperson of the Accounting Research Foundation in Australia (as the AARF was called in 1974), the Secretary of the IASC stated:

> I think it would be unfortunate if the standards for translation issued by the IASC and by the individual accountancy bodies did not agree. Agreement may not be possible, but we should give it a chance. Once standards are issued, they resist change.....Urge the Australian standard setting bodies to consult with their representatives on IASC and with other standard setting Bodies with a view to giving agreement on this issue a chance.[157]

These developments confirm that there was a desire on the part of standard-setting bodies in Australia, Canada, the UK, and to some extent in the US to harmonize standards among theses countries. But the cooperative efforts did not begin until the late 1970's when FAS 8 came under much criticism, leading eventually towards more

---

156 Accounting Standards Review Board Media Release 87/1, April 3, 1987.

157 Letter from Paul Rosenfield to W. John Kenley, October, 24, 1974. In response to the letter, Mr. Kenley did not refer to the issue of agreement (Letter dated October 29, 1974).

harmony in the standards. Beginning in the late 1970's, the standard-setting bodies were heavily influenced by what the other standard-setting bodies were doing. The following section discusses the nature of the discourse on international harmonization. Its effects on the development of foreign currency accounting are not apparent when considering the major differences among the early pronouncements among the countries in this study. However, ultimately, a degree of consensus was achieved. What is of greater interest in this study is the development of harmonization for purposes of facilitating international capital investment to the exclusion of other purposes for harmonization (e.g., monitoring the activities of MNCs by quasi-governmental bodies such as the United Nations) and how that affected who would participate in and benefit from participating in the harmonization process.

The Appeal for Harmonization of Accounting Standards

During the 1960s and early 1970s, there was a movement towards harmonizing accounting techniques and standards worldwide. Several papers refer to an article published in The Journal of Accountancy, January, 1960, as the beginning of this effort[158] in which the author, Jacob Kraayenhof, then senior partner in Klynveld, Kraayenhof, & Co. of Amsterdam (now part of KPMG) and past president of the

---

158 Examples of these papers include: Alvin R. Jennings, "International Standards of Accounting and Auditing", *Journal of Accountancy* (September 1962): 36-42; Alister K. Mason, "The Evolution of International Accounting Standards", in Frederick D. S. Choi, ed., *Multinational Accounting: A Research Framework for the Eighties* (Ann Arbor, Mich.: UMI Research Press, 1981): 155-170; S. M. McKinnon and Paul Janell, "The International Accounting Standards Committee: A Performance Evaluation", *The International Journal of Accounting Education and Research* (Spring 1984): 19-34.

Netherlands Institute of Accountants, was addressing the AICPA at their annual meeting in 1959. In his speech, Mr. Kraayenhof cites some accounting problems common to a number of industrialized countries such as deferred taxes, inflation, revaluation of assets, and depreciation, and points out that while individual countries are unique in their accounting practices, countries do share a number of the same accounting issues to be resolved. He states, for example, "From what I have personally observed, I feel that it is difficult to hold that this problem of changing price levels has different consequences internationally than in the United States."[159] He discusses the problems associated with adjusting financial statements for foreign companies selling their shares in the United States.

> ...the present situation induces corporate management to give one group of shareholders or prospective shareholders a different picture from the one given to other groups of participants and interested parties. I am sure that we all agree that this is fundamentally wrong and therefore unacceptable.[160]

He spoke at a time when no country (except for the United States) had established a "special standing committee" for the development of a set of accounting rules or "generally accepted accounting principles". In a few countries regulations had been issued but many accounting problems were studied by ad hoc committees, whose findings may or may not result in recommendations by the accounting organizations. He states that interested parties "still feel the need of a series of recommendations dealing

---

159 Kraayenhof, *ibid.*

160 *Ibid.*

with other accounting problems". He mentions an attempt to improve financial reporting in the Netherlands in 1955, initiated by the employers' association, which established a committee of executives and managers who made recommendations for the annual report including accounting principles. He illustrates that the accounting profession at that time, not just in his own country but worldwide, lacked the initiative to create some uniformity in accounting standards. But his appeal for uniformity went beyond national accounting rules.

> It is reasonable, of course, that, when selecting one of the various alternatives offered by a set of rules, the choice in any given country is determined by other than purely economic factors; e.g., prevailing political risks or geographical conditions. But the basic principles underlying the financial presentation in each case should be the same.[161]

The speech is an appeal for more uniformity and an established set of guidelines for financial reporting for each country. He emphasizes that the international flow of capital would be facilitated by uniformity in international accounting standards. This is an example of captation in the sense that he presents a reason for harmonization that is difficult to object to. He points out that this is especially crucial for investors buying shares in foreign companies and for foreign subsidiaries reporting to the parent company. Comparable financial data was especially important for facilitating the great number of mergers and amalgamations that were being formed in countries which were members of the Common Market. The Executive Committee of the Common Market was also concerned with comparability of financial data for regulation purposes. However, "The

---

161 *Ibid.*

difficulty of arriving at a reasonable comparability appears repeatedly, because in many cases the accounting principles do not correspond reasonably with each other and/or have not been applied consistently."

Mr. Kraayenhof appeals to the needs of investors, companies listing on foreign exchanges, foreign subsidiaries, merging companies, and regulatory bodies to support his plea for uniformity of accounting standards worldwide. He closed by appealing strongly to the AICPA to take the initiative internationally in the area of accounting principles. His text is an example of discourse that involves persuading the profession and the general public of the importance of providing investors with comparable information on the basis of furthering societal goals (facilitating the flow of capital across national borders).

Similar appeals followed Mr. Kraayenhof's speech. The lack of formal standards for accounting practice in industrial countries and the opportunity this created for the accounting profession was emphasized. Developments such as the expansion of American industry overseas and efforts to reduce trade barriers by the European Common Market were cited as motivations for accountants to help minimize the differences in accounting rules, regulations, principles, and practices:

> The attainment of a general acceptance of over-all accounting postulates and standards and a single and fully comprehended meaning to a certification of financial statements will offer new challenges and greater opportunities for real professional service. The differences between bodies of accountants and the varied interpretations of rules, regulations, principles and practices ought to be minimized as quickly as possible with an eventual goal of uniformity in concepts. Business in every country in its quest for improvement, without regard to national boundaries, will look to the accountant for advice and assistance in all matters of

financial management.[162]

Keller suggests that the accountant's role can, and perhaps should, extend beyond the role of minimizing differences in accounting rules to include building an understanding of profit and profit measurement, influencing the formulation and administration of government policies especially regarding tax structures and tariffs, and fostering a harmonization of wage rates and benefits throughout the world.[163]

That text contributes to the discourse on legitimizing the role of the accounting profession as the experts on what accounting does or should do, so that the task of determining accounting regulation would not fall into the hands of outside parties. This discourse was likely intended not only for the accounting profession, but also to any outside party concerned with the role that accountants serve in order to persuade those parties that accountants are indeed the best authority to establish and maintain rules for providing financial statements. In this way, any party interested in financial information would leave it up to the accountants to determine what information is vital for social needs.

Similarly, the tactic of stacking was used to establish the "fact" of the necessity

---

162

Robert F. Brandt, "One World in Accounting", *The Journal of Accountancy* (July 1962): 68-71. Mr. Brandt was the Consultant to the Committee on Foreign Affairs, U. S. House of Representatives, and former director of the Tokyo and Paris branches of the U. S. General Accounting Office.

163

I. Wayne Keller, "The Accountant's Role in the Expanding International Economy", *Management Accounting* 48 (February 1967): 3-7. Mr. Keller was President and General Manager of International Operations, Armstrong Cork Company, and past President of the National Association of Accountants in the US.

for harmonization of accounting practice in comments made by George W. Ball, senior partner of Lehman Brothers and former U.S. undersecretary of state:

> In an accounting-related sense, there are many developments that suggest the increasing significance of transnational financial reporting: '...foreign holdings of U.S. stocks and bonds are almost 75 percent higher than previous government figures have indicated...the value of such holdings at the end of 1974 was probably $80 billion to $85 billion instead of the $48 billion estimated earlier this year by the Commerce Department.[164] Figures released by the Commerce Department list the total book value of direct investments by foreigners in U.S. industries at almost $22 billion at the start of this year. That is an increase of more than 200 percent since 1960.[165] At December 31, 1974, the New York Stock Exchange had 182 foreign securities listed: 34 foreign stocks and 148 foreign government and private bonds (with a total market value of approximately $15 billion).[166]

The following is an example of fortification (from the same comments) in which the appeal for international accounting standards is justified on the basis of actions taken by various bodies to investigate the activities of MNCs:

> The Securities and Exchange Commission has quietly rejected on several counts an American Stock Exchange proposal to permit foreign corporations to be listed on U.S. exchanges without first having to register with the SEC.[167] The Department of State has recently established an Advisory Committee on Transnational Enterprises....The Committee on Investment and Multinational Enterprises of the Organization for Economic Cooperation and Development [is looking at] the adversary relationship that has arisen between multinational

---

164 *Wall Street Journal,* October 29, 1975, p. 4, cited in Gerhard G. Mueller and Lauren M. Walker, "The Coming of Age of Transnational Financial Reporting", *The Journal of Accountancy* (July 1976): 67-74.

165 *U. S. News and World Report,* December 8, 1975, p. 100, cited in Mueller and Walker, *ibid.*

166 *New York Stock Exchange, 1975 Fact Book,* p. 33, cited in Mueller and Walker, *ibid.*

167 *Wall Street Journal*, November 5, 1975, p. 6, cited in Mueller and Walker, *ibid.*

enterprises and host countries. The lack of any recognized international accounting standards is contributing to the distrust that exists....The Group of Eminent Persons [U.N.] has issued a report, 'The Impact of Multinational Corporations on the Development Process and on International Relations'. Accounting for these business enterprises becomes an integral part of many of the problems discussed. The issue of world standards of accounting will not go away.[168]

These statements illustrate the type of arguments that were used to create the impetus for harmonization and establish the fact that international accounting standards were indeed necessary, thereby creating the interest in establishing the formation of standard-setting bodies such as the IASC. This discourse was directed toward justifying the establishment of these standards in achieving a social purpose, that is, the investigation of MNC activity. The discourse on preserving the legitimacy of the accounting profession served to enhance the perceived interests of investors and creditors. This text is but one example of statements made that contributed to the overall enrollment of any and all parties that might support the efforts toward harmonization of accounting standards. In the end, the justification of investor/creditor interests served to discursively form the interest in international harmonization.

IV. Conclusion

This chapter examined the interest in international harmonization on the part of standard-setting bodies and concludes that, based on the actions of these bodies,

---

168

Remarks of Harvey Kapnick at the Forty-fourth International Conference of the Financial Executives Institute, New Orleans, October 20, 1975, cited in Mueller and Walker, *ibid.*

harmonization was indeed a sought-after goal. The difficulties in achieving complete harmony in the standards may be attributed to the power of certain MNCs to align the interests of the standard-setting bodies with their own. This was concluded on the basis of opportunities that existed for forming networks of alliance between the MNCs and the standard-setting bodies. This was accomplished by the strategic placement of key company personnel, or former personnel, on working parties and task forces which served to align the interests of standard-setting bodies with those of the MNCs. Those companies which placed personnel on working parties on both sides of the Atlantic were the most successful in exerting their influence, despite the resistance by the standard-setting bodies themselves at times and by other MNCs.

Not only were standard-setting bodies dealing with being enrolled in the interests of a few MNCs, they were struggling with establishing or maintaining a sense of legitimacy as independent standard-setting bodies. In the case of Australia, in addition to conflicts with MNCs, particularly mining companies, conflict also arose between standard-setting groups, which resulted in one group enrolling the interests of the other group, who expressed later that they had the same interest all along! Both Australian and Canadian standard-setters were influenced by the actions taken by the FASB and the ASC and were, therefore, influenced indirectly by those standard-setting bodies and the MNCs involved in the processes. The standards that developed were the result of a complex web of strategy and alliance.

The one-dimensional view of power is evident in the interactions between and among MNCs and standard-setting bodies in the development of foreign currency

accounting standards. Particular MNCs exhibited the power to exert their influence over the preferences of other MNCs as they sought to influence the deliberations over the specific provisions of the standards. Conflict among the MNCs as they strived to preserve their preferred methods and engage others to adopt or accept those methods is indicative of one entity getting another entity to do what they otherwise would not do, ie., give up a particular method of accounting translation method for the sake of another. The standard-setting process in the countries under study provided an arena for these MNCs to engage in these activities not only to get other MNCs to accept their preferred methods but also to persuade standard-setting bodies to align with their preferences as well. The results of the deliberation over the standards for foreign currency accounting indicate that those MNCs whose preferences for accounting methods and treatments were adopted by the standard-setting bodies were successful in exerting their power to infuence others.

The different approaches initially adopted by standard-setting bodies may be attributed to the difference in the type of networks that developed in each country. The consensus that later developed may also be contributed to the shifting and changing of networks involving key personnel of MNCs working on task forces. By the establishment of these networks and enrolling the support of the standard-setting bodies, the MNCs were able to stabilize the relations necessary for exercising their power. The resistance exhibited by the MNCs and other interested parties also contributed to the eventual outcomes in the provisions of the standards.

These activities are seen in the context of discourse at the time concerning

harmonization of accounting standards. In the three-dimensional view of power, an entity shapes the desires of other entities so that their expressed preferences align with those of the first entity. The discourse on harmonization can be considered the instrument used to influence standard-setters, MNCs, and other interested parties to not merely develop foreign currency standards but also to harmonize these standards with other countries. The evidence would suggest that both the standard-setting bodies and the MNCs were influenced by this line of thinking. It could be argued that standard-setters might not wish to harmonize in order to preserve their autonomy and that MNCs would not wish for harmony so that they may continue to use their preferred methods. It is not entirely clear where the idea of harmonization originated, thus it is not entirely clear who was trying to shape the wants and desires of standard-setters and MNCs to agree to harmonize. The question of who was behind the movement for harmonization is an open question for further research. Nevertheless, the discourse on harmonization served as an impetus to harmonize foreign currency standards and inadvertently resulted in the preferences of a few MNCs to be adopted. Thus, one may say that accounting standards for foreign currency are the result of a fabrication process involving networks of alliances used to stabilize relations, the resistances to specific provisions that refabricated the standards, and the development of interests involving the harmonization of accounting rules.

CHAPTER 5. CONCLUSION

The collapse of the Bretton Woods agreement in 1973 had implications for many facets of international business. MNCs suddenly had to concern themselves with floating exchange rates which fluctuated wildly relative to the more stable fixed rate system. The implications for accounting standard-setters involved the development of guidelines for translation of balance sheet items and income statements and for treatment of translation and transaction gains and losses. The advent of the floating rate system coincided with a movement to develop mandatory accounting standards (particularly in the US and the UK), as opposed to mere recommendations which had been the pattern previous to the early 1970s. As standard-setting bodies struggled to establish legitimacy for themselves as the organization with the most expertise in developing accounting standards, they were pressured to resolve the foreign currency crisis. Standards for foreign currency accounting arose as a consequence of the dismantling of Bretton Woods, the globalization of business, and a push for harmonization of accounting rules.

These conditions set the stage for the debate on translation methods and treatments of foreign exchange differences. The choices made concerning these methods and treatments by the standard-setting bodies in the US, the UK, Australia, and Canada depended upon a number of factors. These countries shared a similar process for developing accounting standards in which constituents had ample opportunity to respond to releases of exposure drafts via comment letters and public hearings, a process not common among continental European or Asian countries. Furthermore, the standard-

setting bodies in these countries were fairly independent of government influence, unlike other countries in Europe and Asia where government played a more direct role in developing accounting rules and procedures.

Despite the similarities of these countries, different conditions among these countries at first glance may explain the choices made by standard-setting bodies in developing methods of translation and treatments of gains and losses. These factors include various current practices by MNCs that developed ways of coping with the floating rate system, accounting principles originating within the standard-setting body itself or from academic circles, currency fluctuations and trends that could render one method more favourable than another, lobbying efforts by those entities with the most concern with this topic and favouring one method or another, and current and pending tax laws that affect the treatment for gains and losses. Although these factors are consistent with certain outcomes of the deliberations on foreign currency standards, a comparative historical analysis shows that they are not sufficient to explain why certain choices were made by the standard-setting bodies and how consensus among these countries was achieved.

This dissertation has analysed the social relations among standard-setting bodies and specific outside parties to account for the foreign currency standards that evolved. In doing so, this dissertation has probed more deeply into the more subtle, often overlooked, relationships among standard-setting bodies themselves as they struggled for harmonization, relationships that also affected the outcomes of the process of developing standards for foreign currency. The results of the investigation indicate that international

harmonization was very much a sought-after goal of standard-setting bodies but that was difficult to achieve because of differences of rationales and reasons for various provisions of the standards.

The theories on power presented in this dissertation make it easier to understand the process involved in harmonizing foreign currency standards. Consistent with the one-dimensional view of power, conflict was evident among the standard-setting bodies and the MNCs that chose to participate in the process. This evidence contrasts with the facilitative view of power involving the use of authoritative decisions to further collective goals, suggesting that power was not exercised as a capacity or an ability but as a relation. In this case the goal was the harmonization of foreign currency standards. However, the different preferences for specific methods of translation and treatments of gains and losses were the basis for conflict.

What ensued was a series of events involving networks of alliances between certain MNCs and standard-setting bodies. These events are consistent with the one-dimensional view of power in which an entity (or entities) has the capacity to exercise power over another. The MNCs established this capacity by the strategic placement of key personnel that were intricately involved in the establishment of the best methods and treatments to be adopted. These key personnel were seen as experts by the standard-setting bodies in the topic of foreign currency accounting. In some cases the help of these experts was solicited and in other cases it was the experts themselves that asked to serve in some capacity. The result was an infiltration of a particular approach to foreign currency accounting advocated mainly by one MNC, which had effectively convinced

more than one standard-setting body to endorse its methods. In the interest of international harmonization, the approach was eventually adopted by these countries.

The final outcomes, however, were not strictly the preferences of the MNCs involved, but also the result of resistances exhibited by other parties, for example the banks and the Department of Trade in the UK, both which played a role in protesting and affecting certain provisions of the standards. This resistance was also part of the development of these standards because it refabricated the technology and delayed its outcome. The process of fabricating accounting technologies involves not only covert conflict and power struggles between those classes in power and those who are not even aware of their interests in the technology but also overt conflict among those in power. The process of developing foreign currency standards and reaching a level of harmonization reflects these struggles. The dominant power in this process for foreign currency accounting was not MNCs in general, as opposed to other groups that might have had an interest in the subject, but certain MNCs with very specific situations that required, in the minds of the management of these MNCs, that only certain methods and treatments be acceptable. It is from these social and political relations that foreign currency accounting developed.

Consistent with the one-dimensional view of power, foreign currency standards came into being as the result of complex and strategic action involving networks of power for several diverse and sometimes explicable reasons. These standards also developed as a result of some inexplicable reasons. These include what was at stake for the specific MNCs that were involved in the process. While this dissertation attempts to

explain why Unilever, Royal Dutch Shell, DuPont, and ICI were involved and why they preferred their particular methods of accounting, this study does not explain why other MNCs were less involved in the process or not involved at all. The two dimensional view of power would suggest that their preferences or interests might have been excluded from the decision-making process, making it difficult to determine if other entities were in conflict with those whose influence was manifested. Furthermore, this research does not explain why the preferences did not coincide for the MNCs that were involved. Were they really not in favour of harmonization but rather only in their own interests? Could the MNCs even determine whether or not harmonization was in their interests? These unanswered questions are some of the limitations of this study and suggest the need for more in-depth case work on these MNCs to answer them. Another limitation of the study is not showing whether or not, or how, government might have controlled the agenda or created a bias or instilled an attitude of competition among international capital markets that would encourage differences and hamper harmonization for the sake of competition rather than promote a sense of harmony.

The focal point of this dissertation was primarily an analysis of these relations between MNCs and the standard-setting bodies from a one-dimensional view of power. From a two-dimensional perspective, one could investigate why certain MNCs were involved in the process of developing these standards and not others. Were others not interested or were these MNCs considered experts by the standard-setting bodies, thus creating a forum for their preferences and not those of other MNCs to be considered in the debate? This dissertation implies that the MNCs involved may have wanted to exert

their influence in the deliberation, but the case may be that they were chosen by the standard-setting committees for specific reasons.

An attempt was made to show how the discourse of harmonization affected the process of developing these standards. The three-dimensional view suggests that this discourse prevented certain wants or interests to be considered because of the desire to harmonize. Effectively it appears that certain choices (i.e., certain methods and treatments) considered by standard-setting bodies were pre-empted in the spirit of harmonizing with other entities. Further research to investigate the three-dimensional perspective could have been conducted in such a way as to delve more deeply into the nature of standard-setting and investigate, for example, the trend towards mandatory accounting standards and who or what was in favour or opposed to the enforcement or imposition of accounting rules on MNCs and their foreign currency transactions.

In the three dimensional view, A shapes B's wants. The challenge is to investigate who is A and who is B in the story of foreign currency accounting. Another challenge is identifying the wants that were influenced and shaped. Was it the desire to harmonize or was it the desire to set standards for foreign currency in the first place? Would A be the regulatory agencies, such as the SEC, whose influence is felt by capital markets and where the competitive environment is shaped by the enforcement of standards? Is B the investors whose desire for uniformity or harmony in foreign currency accounting was assumed or was it the case that the MNCs were socialized into accepting harmonization? Who else has a stake in the deliberations over accounting methods and treatments? These questions are not easily answered and require some exploratory work

that was beyond the scope of this dissertation, but would provide some insight into the forces or influences that shape accounting developments.

This research builds on Lukes and Gaventa, who seek to explain social processes of resolving issues and how outcomes of those processes develop. This study seeks to explain why different social entities prefer different solutions to a worldwide problem but then decide to strive for a solution common to all. The development for foreign currency standards can be seen as an interaction of social entities acting on a technical subject while being influenced by the social discourse of the time, the harmonization of accounting standards.

BIBLIOGRAPHY

Abbott, Nancy L., "Translation of Long-Term Debt: The Book and Tax Consequences", *International Tax Journal* 5 (February 1979): 227-230.

Accounting Standards Committee, "ED 27: Accounting for Foreign Currency Translations", *Accountancy* (December 1980): 119-126.

_____, "SSAP 20: Foreign Currency Translation", *Accountancy* 94 (May 1983): 120-128.

Aglietta, Michel, *A Theory of Capitalist Regulation* (London: New Left Books, 1979).

Alexander, David, and Simon Archer, *European Accounting Guide* (London: Harcourt Brace Jovanovich, 1991).

Amernic, Joel H., and Brian J. B. Galvin, " Foreign Currency Translation: The Debate Goes On", *CA Magazine* (March 1982): 30-37.

Arendt, Hannah, *On Violence* (London: The Penguin Press, 1970).

Arnold, Jerry L., and William W. Holder, *Impact of Statement 52 on Decisions Financial Reports and Attitudes* (Morristown, NJ: Financial Executives Research Foundation, 1986).

Australian Accounting Research Foundation, ED 11, *Proposed Statement of Accounting Standards: "Translation of Foreign Currency Transactions and Foreign Currency Financial Statements in the Context of Historical Cost Accounting"* (June 1979).

Australian Society of Accountants and the Institute of Chartered Accountants in Australia, ED 4, *Proposed Statement of Accounting Standards: "Translation of Amounts in Foreign Currencies"* (September 1973).

Bachrach, P., and M. S. Baratz, "Decisions and Non-decisions: An Analytical Framework" *American Political Science Review* (1963):641-51.

_____, *Power and Poverty: Theory and Practice* (Oxford: Oxford University Press, 1970).

Benton, T., "'Objective Interests and the Sociology of Power", *Sociology* 15(2) (1981):161-84.

Beresford, Dennis, and D. Neary, "FASB slates major changes to statement No. 8," *Financial Executive* 47 (September 1979): 6.

Black, Stanley W., *Floating Exchange Rates and National Economic Policy* (London: Yale University Press, 1977).

Block, Fred L., *The Origins of International Economic Order: A Study of United States International Monetary Policy from World War II to the Present* (Berkeley: University of California Press, 1977).

Bloom, Robert, and M. A. Naciri, "Accounting Standard Setting and Culture: A Comparative Analysis of the United States, Canada, England, West Germany, Australia, New Zealand, Sweden, Japan, and Switzerland", *The International Journal of Accounting* 24 (1989): 70-97.

Buell, Frederick, *National Culture and the New Global System* (Baltimore: Johns Hopkins University Press, 1994).

Burchell, Stuart, Colin Clubb, Anthony Hopwood, John Hughes, and Janine Nahapiet, "The Role of Accounting in Organizations and Society", *Accounting, Organizations and Society* 5 (1980): 5-27.

Business Review Weekly, "Miner Fail in Forex Write-off Bid", December 20, 1985.

Brandt, Robert F.,"One World in Accounting", *The Journal of Accountancy* (July 1962): 68-71.

Bryant, M. J., "Formal Lobbying Activity: The Case of FAS 8," Working paper (University of Toronto, 1988).

Cairns, David, "Time for turf warriors to reach a peace accord", *Financial Times* (May 16, 1996).

Choi, Frederick D. S., Howard D. Lowe, and Reginald G. Worthley, " Accountors, Accountants, and Standard No. 8," *Journal of International Business Studies* (Fall 1978): 81-87.

Choi, Frederick D. S., and Gerhard G. Mueller, *International Accounting, 2nd Edition* (Englewood Cliffs, NJ: Prentice-Hall, 1992).

Choi, Frederick D. S., and J. Matthew Singleton, "Accounting for Derivative Products", in Frederick D. S. Choi, ed., *Handbook of International Accounting* (New York: John Wiley & Sons, Inc., 1991).

CICA, *Financial Reporting in Canada,* 12th edition (Toronto: CICA, 1977).

_____, *Financial Reporting in Canada,* 14th edition (Toronto: CICA, 1981).

_____, *Financial Reporting in Canada,* 15th edition (Toronto: CICA, 1983).

_____, "Translation of foreign currency transactions and foreign currency financial statements", *CICA Handbook* Section 1650, 1978, para. 1650.45.

CICA Accounting Research Committee, *Foreign Currency Translation,* Exposure Draft, June 1982.

Cliffe, Lionel, "Modern World Capitalism and its Contemporary Crisis", in David Coates and Gordon Johnston, eds., *Socialist Strategies* (Oxford: Martin Robertson, 1983).

Consultative Committee of Accountancy Bodies, "Borrowings in Foreign Currency", TR 209, memorandum submitted to the Board of Inland Revenue, December 1976.

Coopers & Lybrand, *International Accounting Summaries: A Guide for Interpretation and Comparison* (New York: John Wiley & Sons, 1991).

Dahl, Robert A., "The Concept of Power", 2 *Behavioral Science* (1957):201-205.

_____, "A Critique of the Ruling Elite Model", *American Political Science Review* 52 (1958): 463-469.

_____, *Who Governs? Democracy and Power in an American City* (New Haven and London: Yale University Press, 1961).

Daley, Lane A., and Terry Tranter, "Limitations of the Value of the Conceptual Framework in Evaluating Extant Accounting Standards", *Accounting Horizons* (March 1990): 15-24.

Deupree, Marvin M., "Translating Foreign Currency Financial Statements to U. S. Dollars", *Financial Executive* (October 1972): 48-68.

Dormael, Armand Van, *Bretton Woods: Birth of a Monetary System* (New York: Holmes & Meier Publishers, Inc., 1978).

Drummond, Christina S. R., *Foreign Currency Translation* (Toronto: Butterworths, 1983).

Dunne, Paul, "Foreign Currency Translation at Alcan", *CA Magazine* (October 1983): 40-49.

Economist, "Bean counters, Unite!" *The Economist* (June 10, 1995): 67-68.

_____, "The Nation-State is Dead, Long Live the Nation-State", *The Economist* (December 23rd 1995-January 5th 1996): 15-18.

_____, "Global accounting's roadblock", *The Economist* (April 27, 1996): 79-80.

Eddey, Peter H., and Frank W. Johnson, "Exchange Rates, Foreign Borrowings and Profit Distortion", *The Chartered Accountant in Australia* 53 (October 1982): 22-25.

Falk, Haim, "International Accounting: A Quest for Research", *Contemporary Accounting Research* 11 (Fall 1994): 595-615.

Fantl, Irving L., "Problems with Currency Translation--A Report on FASB No. 8," *Financial Executive* (December 1979): 33-36.

FASB, *FASB Discussion Memorandum: An Analysis of Issues Related to Accounting for Foreign Currency Translation* (Stamford, CT: FASB) February 21, 1974.

_____, *Exposure Draft: Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements* (Stamford, CT: Financial Accounting Standards Board, December 31, 1974).

_____, *Statement of Financial Accounting Standards No. 8: Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements* (Stamford, CT: Financial Accounting Standards Board, October, 1975): para. 125.

_____, *Statement of Financial Accounting Standards No. 52: Foreign Currency Translation* (Stamford, CT: FASB, December 1981).

FASB News Release, "Financial Accounting Standards Board Places 7 Subjects on Initial Agenda" (Stamford, CT: FASB, April 5, 1973).

_____, "FASB Task Forces Appointed for Foreign Currency Translation, Reporting by Diversified Companies" (Stamford, CT: FASB, May 31, 1973).

FASB Research Staff, "A Study of Disclosure of Foreign Currency Translation Information" (December 1973).

FASB, *Financial Accounting Series: Status Report No. 284* (January 14, 1997).

Financial Executives Institute, Committee on Corporate Reporting, Foreign Exchange Conversions Subcommittee, "Survey of U.S. Company Foreign Translation Practices" (October 31, 1973).

Fitzergerald, Richard D., "International Harmonization of Accounting and Reporting", *The International Journal of Accounting Education and Research* (Fall 1981): 21-32.

Foucault, Michel, "Questions of Method", in Graham Burchell, Colin Gordon, and Peter Miller, eds., *The Foucault Effect: Studies in Governmentality* (Chicago: University of Chicago Press, 1991).

Fujita, Yukio, "Recent Activities of the United Nations toward International Harmonization in Accounting and Reporting", in *Changing International Financial Markets and Their Impact on Accounting* (Champaign, Ill.: Centre for International Education and Research in Accounting, Dept. of Accoutancy, 1992).

Gaventa, John, *Power and Powerlessness: Quiescence and Rebellion in an Appalachian Valley* (Urbana, Ill.: University of Illinois Press, 1980).

Gernon, Helen, and R. S. Olusegun Wallace, "International Accounting Research: A Review of its Ecology, Contending Theories and Methodologies", *Journal of Accounting Literature* 14 (1995): 54-106.

"Getting to grips with accounting Standards", *Accountancy* 90 (September 1979):22.

Giddens, A. *New Rules of Sociological Method* (London: Hutchinson, 1976).

_____, *Studies in Social and Political Theory* (London: Hutchinson, 1977).

_____, *Central Problems in Social Theory* (London: Macmillan, 1979).

_____., *A Contemporary Critique of Historical Materialism* (London: Macmillan, 1981).

_____, *The Constitution of Society* (Cambridge: Polity Press, 1984).

Globe and Mail, "Accounting Rule Distorts Multi-nationals' Reporting", *Globe and Mail* (August 6, 1981).

Griffin, P. A., "Foreign Exchange Gains and Losses: Impact on Reported Earnings", *Abacus* 18 (June 1982): 50-69.

_____, "Managements' Preferences for FASB Statement No. 52: Predictive Ability Results", *Abacus* 19 (1983): 130-138.

Habermas, J., "Toward a Theory of Communicative Competence", *Inquiry* 13 (1970): 360-75.

_____, *Knowledge and Human Interests* (London: Heineman Educational Books, 1972).

_____., *Legitimation Crisis* (London: Heineman Educational Books, 1976).

Haring, J. R., "Accounting Rules & 'The Accounting Establishment'", *Journal of Business* (1979): 507-520.

Harris, Trevor S., "Foreign Currency Transactions and Translations", in Frederick D. S. Choi, ed., *Handbook of International Accounting* (New York: John Wiley & Sons, 1991).

Held, David, "Introduction: Central Perspectives on the Modern State", in David Held, James Anderson, Bram Gieben, Stuart Hall, Laurence Harris, Paul Lewis, Noel Parker, and Ben Turok, eds., *States and Societies* (Oxford: Martin Robertson & Co., Ltd., 1983).

Hinton, P. Raymond, "Foreign Currency Translation: Conceptual and Practical Limitations of the Currency Rate Method", *The Accountant* 178 (May 4, 1978): 591-592.

Hobsbawn, Eric J., *Nations and Nationalism since 1789: Programme, Myth, Reality* (Cambridge: Cambridge University Press, 1990).

Hope, Anthony, and John Briggs, "Accounting Policy-Making: Some Lessons from the Deferred Taxation Debate", *Accounting & Business Research* (1982): 83-96.

Hope, Anthony, and Rob Gray, "Power and Policy Making: The Development of an 'R & D' Standard", *Journal of Business Finance and Accounting* (1982): 83-96.

Houston, Carol Olson, "Foreign Currency Translation Research: Review and Synthesis", *Journal of Accounting Literature* 8 (1989): 25-48.

Hussein, M. E., and J. C. Ketz, "Ruling Elites of the FASB: A Study of the Big Eight", *Accounting Review* (1980): 354-367.

IASC, Exposure Draft 11, *Accounting for Foreign Transactions and Translation of Foreign Financial Statements* (London: IASC, 1977).

_____, Exposure Draft 23, *Accounting for the Effects of Changes in Foreign Exchange Rates* (London: IASC, 1982).

ICAEW, Accounting Standards Committee, "Exposure Draft 21-Accounting for foreign currency transactions", *Accountancy* 88 (October 1977): 75-79.

Jansz, Rodney, "Foreign Currency Translation--The Continuing Debate", *The Chartered Accountant in Australia* 55 (July 1984): 40-41.

Jennings, Alvin R., "International Standards of Accounting and Auditing", *Journal of Accountancy* (September 1962): 36-42.

Johnson, S. B., and D. Solomons, "Institutional Legitimacy and the FASB", *Journal of Accounting and Public Policy* 3(2) (1984): 165-183.

Journal of Accountancy, "IASC Issues Second Draft on Translation", 153 (March 1982): 20.

Kay, J., and J. King, *Taxing Currency Fluctuations? The Tax Treatment of Foreign Exchange Gains and Losses* (London: The Institute for Fiscal Studies, 1985).

Keiso, Donald E., and Jerry J. Weygandt, *Intermediate Accountings, Seventh Edition* (New York: John Wiley & Sons, Inc., 1992).

Keller, I. Wayne, "The Accountant's Role in the Expanding International Economy", *Management Accounting* 48 (February 1967): 3-7.

Kelly, Lauren, "Corporate Lobbying and Changes in Financing or Operating Activities in Reaction to FAS No. 8," *Journal of Accounting and Public Policy* (Winter 1982): 153-73.

_____, "Corporate Management Lobbying on FAS No. 8: Some Further Evidence", *Journal of Accounting Research* 23 (Autumn 1985): 619-632.

Kenley, W. J., "Points from Published Accounts. Reporting of Foreign Currency Transactions", *The Chartered Accountant in Australia* (March 1978): 38-43.

Kenny, Sara York, and Robert K. Larson, "The Development of International Accounting Standards: An Analysis of Constituent Participation in Standard-Setting", *The International Journal of Accounting* 30 (1995): 283-301.

Kirsch, Robert J., and Dawn Becker-Dermer, "Proposed Revisions of International Accounting Standard No. 21 and their Implications for Translation Accounting in Selected Countries:The US, the UK, Australia, and Canada", *International Journal of Accounting* 30 (1995): 1-24.

Kirsch, Robert J., Thomas G. Evans, and Timothy S. Doupnik, "FASB Statement 52, An Accounting Policy Intervention: U. S.-Based Multinational Corporate Preenactment Lobbying Behavior", *Advances in International Accounting* 3 (1990): 155-171.

Kligman, Jonathan M., "Foreign currency translation: from exposure draft to standard", *CA Magazine* (June 1983): 57-60, 62.

Kraayenhof, Jacob, "International Challenges for Accounting", *Journal of Accountancy* (January 1960): 34-38.

Kroneberger, Dr. Wolf, and Peter H. Combrink, *Accounting and Auditing in Germany* (Frankfurt, Germany: Coopers & Lybrand, 1991).

Kubin, Konrad, "Accounting for Foreign Currency Translations: Current Problems in Historical Perspective", *Accounting Historians Journal* 2 (1975): 11-16.

Largay, James A., "SFAS No. 52: Expediency or Principle?" in Jagdish Sheth and Abdolreza Eshghi, eds., *Global Accounting Perspectives* (Cincinnati, OH: South-Western Publishing Co., 1989).

Lash, Scott, and John Ury, *The End of Capitalism* (Madison, WI: University of Wisconsin Press, 1987).

Latour, Bruno, *Science in Action* (Cambridge, MA: Harvard University Press, 1987).

Laughlin, Richard C., and Anthony G. Puxty, "Accounting Regulation: An Alternative Perspective", *Journal of Business Finance & Accounting* 10 (1983): 451-479.

Law, John, "Introduction: monsters, machines and sociotechnical relations", in John Law (ed.), *A Sociology of Monsters: Essays on Power, Technology and Domination* (London: Routledge, 1991a): 1-23.

Lijphart, Arend, "Comparative Politics and the Comparative Method", *American Political Science Review* 65 (1971): 682-693.

Lipietz, Alain, *Towards a New Economic Order: Postfordism, Ecology and Democracy* (New York: Oxford University Press, 1992).

Lukes, S., *Power: A Radical View* (London: Macmillan, 1974).

Mason, Alister K., "The Development of International Financial Reporting Standards", *ICRA Occasional Paper No. 17* (Lancaster, England: International Center for Research in Accounting, University of Lancaster, 1978).

_____, "The Evolution of International Accounting Standards", in Frederick D. S. Choi, ed., *Multinational Accounting: A Research Framework for the Eighties* (Ann Arbor, Mich.: UMI Research Press, 1981): 155-170.

Mauer, Laurence J., "MNCs Gain New Freedom Under FAS 52 Flexibility", *Management Accounting* (December 1983): 30-33.

McCallum, John S., "Foreign Currency Borrowing: The Canadian Perspective", *CGA Magazine* (April 1977): 3-6.

McComb, Desmond, "International Accounting Standards and the EEC Harmonization Program: A Conflict of Disparate Objectives", *The International Journal of Accounting, Education and Research* (Spring 1982): 35-48.

McKinnon, S. M., and Paul Janell, "The International Accounting Standards Committee: A Performance Evaluation", *The International Journal of Accounting Education and Research* (Spring 1984): 19-34.

Messier, William F., Jr., "SFAS No. 8: Some Implications for MNCs", *The International Journal of Accounting Education and Research* (Spring 1979): 101-119.

Mill, John Stuart, *A System of Logic*, 8th ed. (London: Longmans, Green, Reader, & Dyer, 1872).

Miller, Peter, and Nikolas Rose, "Governing Economic Life", *Economy and Society* 19 (February 1990): 1-69.

Moore, David J., "Foreign Currency Translation", *CA Magazine* (September 1977): 63-66.

_____, "Foreign Currency Translation", *CA Magazine* (September 1978): 76-80.

Moore, Michael L., and John L. Kramer, "Taxation and Accounting Rules for Currency Translation", *International Tax Journal* 3 (February 1977): 238-73.

Morgan, Glenn, "The Global Context of Financial Services: National Services and the International Political Economy", in G. Morgan and D. Knights, eds., *Deregulation and European Financial Services* (London: Macmillan, forthcoming).

Mueller, Gerhard G., "Are Traditional Foreign Exchange Translation Methods Obsolete?" *California Management Review* 7 (Summer 1965): 41-46.

_____, "1992 and Harmonization Efforts in the EC", in Frederick D. S. Choi, ed., *Handbook of International Accounting* (New York: John Wiley & Sons, 1991).

Mueller, Gerhard G., and Lauren M. Walker, "The Coming of Age of Transnational Financial Reporting", *The Journal of Accountancy* (July 1976): 67-74.

New York Stock Exchange, 1975 Fact Book.

Nobes, C. W., "A Review of the Translation Debate", *Accounting and Business Research* (Autumn 1980): 421-431.

OECD Economic Outlook, July, 1973.

OECD Economic Outlook, December, 1979.

OECD Economic Outlook, 1989.

Ogus, A., *Regulation: Legal Theory and Economic Forms* (Oxford: Oxford University Press, 1994).

Parker, R. H., "Principles and Practice in Translating Foreign Currencies: An Essay in Comparative Accounting", *Abacus* 6 (December 1970): 144-153.

Parkinson, R. MacDonald, "The Floating Dollar", *Canadian Chartered Accountant* (January 1971): 59-63.

_____, *Translation of Foreign Currencies* (Toronto: CICA, 1972).

Parsons, R. W., *Income Taxation in Australia* (Melbourne: The Law Book Company Ltd, 1985): 424-427, 747-754.

Parsons, Talcott,"The Distribution of Power in American Society", *World Politics* 10 (October 1957): 123-143.

_____,"On the Concept of Influence", *Public Opinion Quarterly* 27 (1963a): 37-62.

_____, "On the Concept of Political Power", *Proceedings of the American Philosophical Society* 107 (1963b):232-262.

_____, *Sociological Theory and Modern Society* (New York: The Free Press, 1967)

Peckron, Harold S., "Tax Consequences of Currency Futures After *Hoover* ", *International Tax Journal* 6 (1980): 165-177.

Portington, Michael, "Foreign Currency Translation: The New Accounting Approach", *Accountancy* (February 1981): 105-107.

Preston, Alistair M., David J. Cooper, and Rod W. Coombs, "Fabricating Budgets: A Study of the Production of Management Budgeting in the National Health Service", *Accounting, Organisations and Society* 17 (1992): 561-593.

Public Record Discussion Memorandum on Accounting for Foreign Currency Translation--dated February 21, 1974 (Stamford, CT: FASB, 1974).

Rickard, D. R., "Currency Translation", *The Australian Accountant* 50 (January/February): 10-11.

Riper, Robert Van, *Setting Standards for Financial Reporting: FASB and the Struggle for Control of a Critical Process* (Westport, CT: Quorum Books, 1994).

Rivera, Juan M., "The Internationalization of Accounting Standards: Past Problems and Current Prospects", *The International Journal of Accounting Education and Research* 24 (1989): 320-341.

Robson, Keith, "On the Arenas of Accounting Change: The Process of Translation", *Accounting, Organisations and Society* 16 (1991): 547-570.

Robson, Keith, and D. J. Cooper, "Power and Management Control", in W. F. Chua, E. A. Lowe, and A. G. Puxty, eds., *Critical Perspectives in Management Control* (London: Macmillan, 1989): 79-114.

Roof, Bradley M., "FASB No. 8--Did it Help or Hinder Multinational Reporting?", *Financial Executive* 50 (March 1982): 27-36.

Rueschhoft, N. B., *International Accounting and Financial Reporting* (Praeger: 1976), in David J. Cooper and Michael J. Sherer, "The Value of Corporate Accounting Reports: Arguments for a Political Economy of Accounting", *Accounting, Organizations and Society* 9 (1984): 207-232.

Saltoun, Andre M., "Tax Aspects of International Exchange Transactions", *Proceedings from the 40th Annual N. Y. Institute on Federal Taxation* (1982).

Savoie, Leonard M., "Financial and Accounting Aspects in International Business", *The International Journal of Accounting Education and Research* 9 (1973): 13-22.

Scott, David A., and Bryan C. Walker, "Foreign Currency Translation in Canada and the U. S.", *CA Magazine* 10 (November 1977): 48-53.

Seidler, Lee J., "An Income Approach to the Translation of Foreign Currency Financial Statements", *The CPA Journal* 42 (January 1972): 26-35.

Serfass, William D., Jr., "Possible Undesirable Effects of FASB No. 8," *CPA Journal* 46 (May 1976): 59.

Sewell, William H., "Marc Bloch and the Logic of Comparative History", *History and Theory* 6 (1967): 208-218.

Skocpol, T., *States and Social Revolutions: A Comparative Analysis of France, Russia and China* (Cambridge: Cambridge University Press, 1980): 36-40.

_____, "Emerging Agendas and Recurrent Strategies in Historical Sociology", in Theda Skocpol, ed., *Vision and Method in Historical Sociology* (Cambridge: Cambridge University Press, 1984): 356-391.

Smelser, Neil J., *Comparative Methods in the Social Sciences* (Englewood Cliffs, N. J.: Prentice-Hall, 1976).

Smith, Alan F., "Temporal Method: Temporary Mode?", *Management Accounting* 59 (February 1978): 21-26.

Solomons, D. S., *Making Accounting Policy: The Quest for Credibility in Financial Reporting* (Oxford, 1986).

Spector, Stephen, "Standards Update", *CGA Magazine* (August 1982): 5.

Stanley, Marjorie T., and Stanley B. Block, "Response by United States Financial Managers to Financial Accounting Standard No. 8," *Journal of International Business Studies* (Fall 1978): 89-99.

Sutton, Michael H., "Financial Reporting in U. S. Capital Markets: International Dimensions", *Accounting Horizons* 11 (June 1997): 96-102.

Tandy, P. R., and N. L. Wilburn, "Constituent Participation in Standard-setting: The FASB's First 100 Statements", *Accounting Horizons* 6 (1992): 47-58.

Taylor, Graham D., and Patricia E. Sudnik, *DuPont and the International Chemical Industry* (Boston: Twayne Publishers, 1984).

Tew, Brian, *The Evolution of the International Monetary System: 1945-85*, 3rd ed. (London: Hutchinson, 1985).

Tugendhat, Christopher, *The Multinationals* (New York: Pelican Books, 1984).

U. S. News and World Report, December 8, 1975.

Vann, Richard J., and Ross W. Parsons, "The Foreign Tax Credit and Reform of International Taxation", *Australian Tax Forum* 3 (1986): 202-211.

Wall Street Journal, October 29, 1975.

_____, November 5, 1975.

Wallace, P., and B. D. G. Ogle, "Foreign Currency Translation", *Selected Accounting Standards--Interpretation Problems Explained* (London: ICAEW, 1984): 201-254.

Watts, R. L., and J. Zimmerman, "Towards a Positive Theory of the Determination of Accounting Standards", *Accounting Review* 53 (January 1978): 112-134.

Weir, M., and T. Skocpol, "State Structures and the Possibilities for 'Keynesian Responses to the Great Depression in Sweden, Britain, and the United States", in P. B. Evans, D. Rueschemeyer, and T. Skocpol (eds.), *Bringing the State Back In* (Cambridge: Cambridge University Press, 1985): 107-163.

White, Michael J., "Isolated Foreign Currency Transactions and Foreign Exchange Futures Contracts", in *Report of Proceedings of the Thirtieth Tax Conference*, Canadian Tax Foundation, Montreal, 20-22 November 1978.

Willey, Russell W., *Foreign Exchange: The Accounting, Economics, and Control* (Wilmington, DE: Nopoly Press, Inc., 1977).

_____, "In Defense of FAS No. 8," *Management Accounting* 61 (December 1979): 36-40.

Wilson, Charles, *Unilever 1945-1965: Challenge and Response in the Post-War Industrial Revolution* (London: Cassell, 1968).

Wojciechowski, Stanley R., "DuPont Evaluates FAS 52," *Management Accounting* (July 1982): 30-35.

Wolfinger, R. E. "Nondecisions and the Study of Local Politics", *American Political Science Review* 65 (1971a): 1063-80.

_____, "Rejoinder to Frey's Comment", *American Political Science Review* 65 (1971b): 1102-04.

Woodiwiss, Anthony, *Postmodernity USA: The Crisis of Social Modernism in Postwar America* (London: Sage Publications, 1993).

Wyatt, Arthur R., "International Accounting Standards and Organizations: Quo Vadis?", in Frederick D. S. Choi, ed., *Handbook of International Accounting* (New York: John Wiley & Sons, 1992).

Yamakawa, Thomas T., "How the Strong Yen Influenced Financial Reporting in Japan", *Management Accounting (NAA)* 60 (June 1979): 26-31.

APPENDIX I. MILL'S METHODS

From Theda Skocpol, "Emerging Agendas and Recurrent Strategies in Historical Sociology", in Theda Skocpol, ed., *Vision and Method in Historical Sociology* (Cambridge: Cambridge University Press, 1984): 356-391.

Mill's Methods:

1. Method of Agreement

	Case 1	Case 2	Case n
Overall differences	A	D	G
	B	E	H
	C	F	I
Crucial similarity	X	X	X
Outcomes	Y	Y	Y

In this method, outcomes (Y) are all the same among the cases. A through I represent differing characteristics of the cases, each row depicting a certain characteristic (i.e., A, D, and G are one particular characteristic, B, E, and H are another, etc.). In this method, each case differs among these characteristics. The crucial similarity (X) is the one characteristic is which each case is similar, and hence may explain why the outcomes are the same.

2. Method of Difference

	Case 1	Case 2	Case n
Overall similarities	A	A	A
	B	B	B
	C	C	C
Crucial difference	X	Z	W
Outcomes	Y	T	S

In this method, the outcomes (Y, T, and S) are different among the cases. Characteristics that are the same for each case are depicted by the three rows of overall similarities. Again, each row is a particular characteristic. The crucial differences (X, Z, and W) are the focal point of the study which may explain why the outcomes are different.

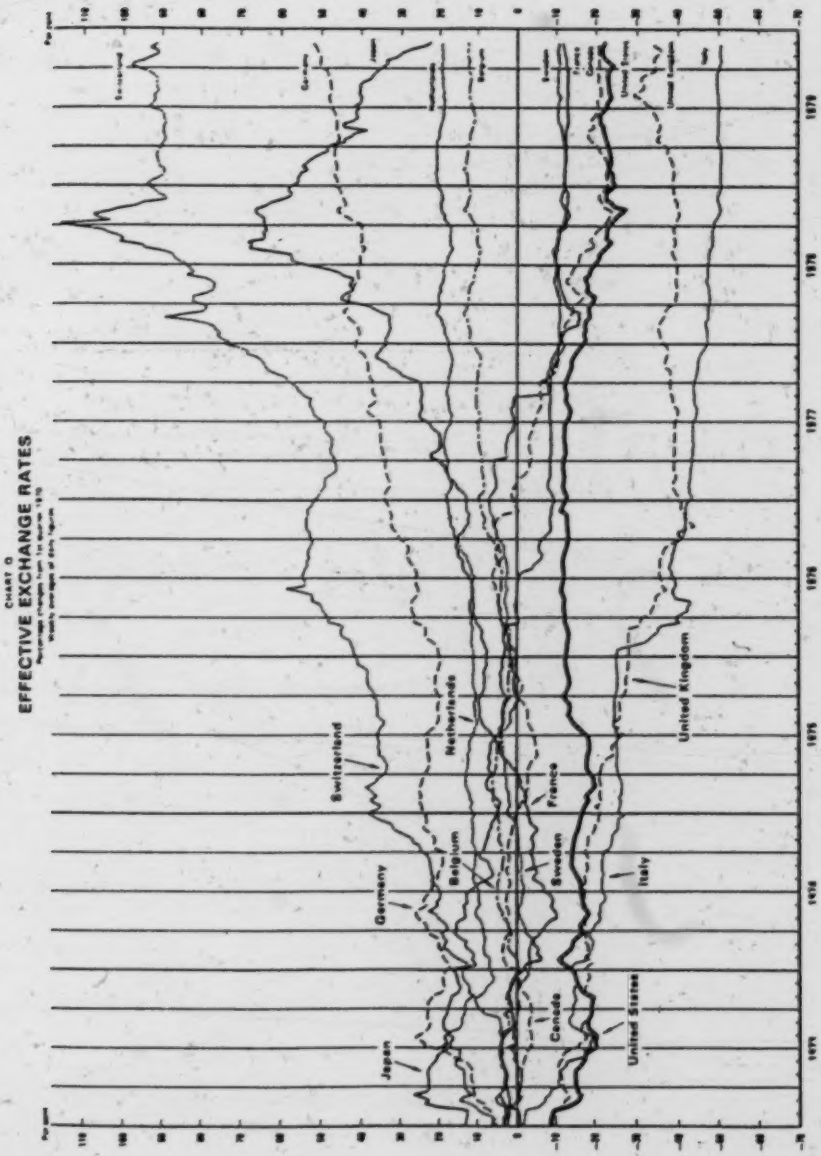
APPENDIX IIA. EXCHANGE RATES, NATIONAL CURRENCIES AGAINST THE UNITED STATES DOLLAR (Reprinted from *OECD Economic Outlook* (June 1989)).

Table R 21 Exchange rates, national currencies against the United States Dollar

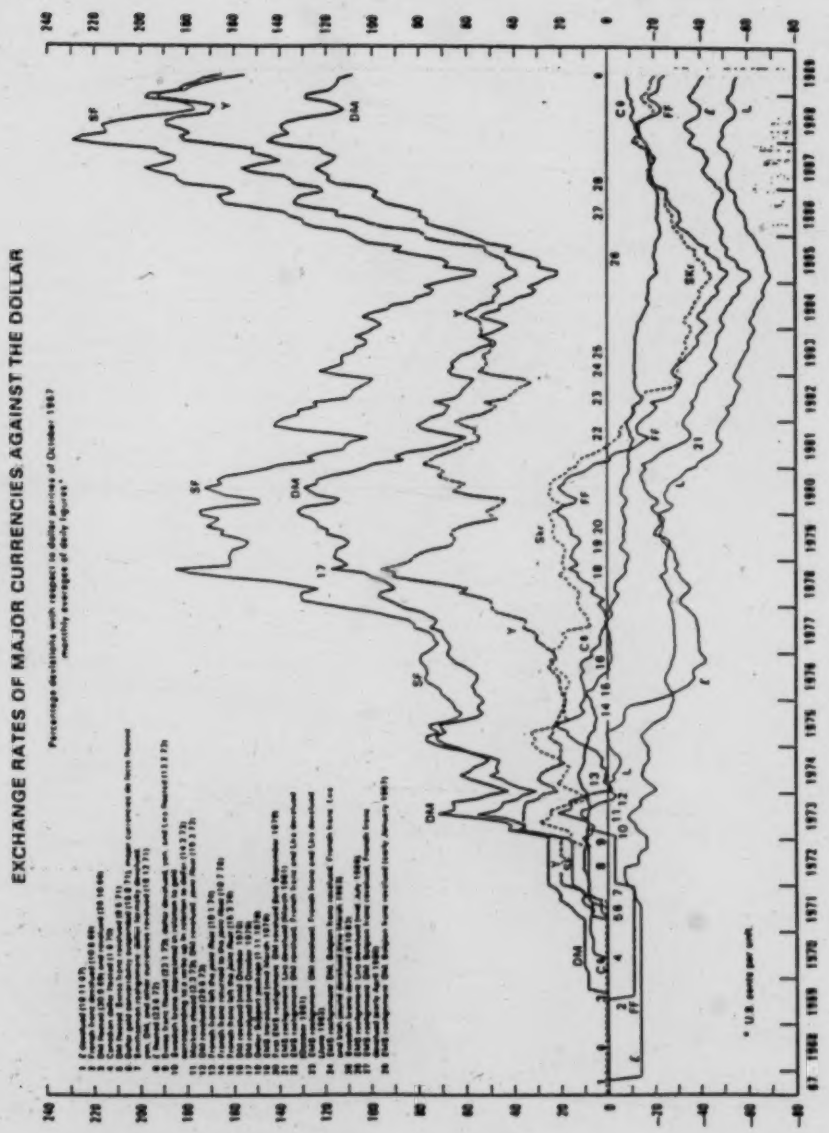
Average of daily rates

	Monetary unit	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988
United States	Dollar	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000
Japan	Yen	291.8	296.5	296.5	268.5	210.4	219.2	226.7	220.6	249.1	237.5	237.6	238.6	168.5	144.6	128.2
Germany	Deutschemark	2.586	2.460	2.510	2.322	2.009	1.833	1.817	2.256	2.427	2.553	2.846	2.944	2.172	1.791	1.756
France	Franc	4.809	4.287	4.780	4.913	4.253	4.216	4.434	5.432	6.572	7.621	8.739	8.984	6.927	6.009	5.956
Italy	Lira	650	653	832	882	849	831	856	1137	1353	1519	1757	1909	1491	1297	1302
United Kingdom	Pound	0.427	0.452	0.557	0.523	0.521	0.432	0.430	0.498	0.533	0.660	0.752	0.779	0.682	0.612	0.562
Canada	Dollar	0.978	1.017	0.986	1.063	1.141	1.171	1.169	1.199	1.233	1.232	1.295	1.366	1.389	1.326	1.231
Austria	Schilling	18.48	17.42	17.94	16.52	14.53	13.37	12.94	15.92	17.06	17.97	20.01	20.69	15.22	12.64	12.34
Belgium-Luxembourg	Franc	38.96	36.79	38.61	35.84	31.50	29.31	29.25	35.14	45.70	51.13	57.76	59.43	44.68	37.34	36.77
Denmark	Krone	6.09	5.74	6.04	6.00	5.51	5.26	5.64	7.12	8.33	9.14	10.36	10.59	8.09	6.84	6.73
Finland	Markka	3.763	3.669	3.856	4.021	4.107	3.887	3.720	4.304	4.813	5.565	6.003	6.196	5.070	4.396	4.186
Greece	Drachma	30.0	32.0	36.5	38.4	35.7	37.0	42.6	55.3	66.7	87.9	112.7	138.1	139.5	135.2	141.4
Iceland	Krona	0.99	1.53	1.82	1.99	2.31	3.51	4.80	7.21	12.30	24.85	31.73	41.54	41.10	38.48	43.03
Ireland	Pound	0.427	0.452	0.557	0.523	0.521	0.489	0.487	0.622	0.704	0.805	0.823	0.946	0.747	0.612	0.657
Netherlands	Guilder	2.688	2.550	2.644	2.455	2.164	2.006	1.988	2.495	2.870	3.154	3.200	3.322	2.450	2.026	1.977
Norway	Krone	5.523	5.223	5.457	5.322	5.241	5.063	4.933	5.732	6.451	7.396	8.160	8.582	7.392	6.737	6.517
Portugal	Escudo	21.2	25.5	30.1	38.2	43.9	45.9	50.0	61.5	79.4	110.8	144.4	169.9	148.2	140.8	143.9
Spain	Peseta	57.6	57.4	66.9	74.0	76.7	67.2	71.7	92.3	109.8	141.5	160.8	170.1	140.0	122.5	116.5
Sweden	Krona	4.433	4.151	4.357	4.481	4.517	4.287	4.229	5.060	6.282	7.667	8.273	8.602	7.124	6.340	6.129
Switzerland	Franc	2.979	2.582	2.500	2.404	1.788	1.663	1.676	1.966	2.030	2.099	2.350	2.457	1.798	1.491	1.463
Turkey	Lira	14	14	16	18	24	36	76	110	161	224	363	520	669	855	1419
Australia	Dollar	0.693	0.760	0.816	0.900	0.893	0.893	0.877	0.869	0.986	1.109	1.141	1.432	1.496	1.428	1.281
New Zealand	Dollar	0.708	0.826	0.998	1.025	0.961	0.978	1.027	1.153	1.332	1.496	1.767	2.026	1.917	1.665	1.529
Singapore	Dollar	2.437	2.371	2.471	2.439	2.224	2.175	2.141	2.113	2.140	2.113	2.133	2.200	2.177	2.106	2.013
Taiwan	Dollar	38.0	38.0	38.0	38.0	37.1	36.0	36.0	37.0	39.0	40.1	39.6	39.8	37.8	31.8	28.5
South Korea	Won	484.5	484.0	484.0	484.0	484.0	484.0	607.4	681.0	731.1	775.7	806.0	870.0	881.0	825.0	730.3
Hong Kong	Dollar	5.032	4.935	4.905	4.642	4.484	5.003	4.936	5.589	6.070	7.765	7.818	7.791	7.803	7.798	7.806

APPENDIX IIB. EFFECTIVE EXCHANGE RATES, PERCENTAGE CHANGES FROM 1ST QUARTER 1970 (Reprinted from *OECD Economic Outlook* (December 1979)).



APPENDIX IIC. EXCHANGE RATES OF MAJOR CURRENCIES AGAINST THE DOLLAR (Reprinted from *OECD Economic Outlook* (June 1989)).



APPENDIX III. INFLATION EFFECTS OF TRANSLATION METHODS

From J.Kay and J. King, *Taxing Currency Fluctuations? The Tax Treatment of Foreign Exchange Gains and Losses* (London: The Institute for Fiscal Studies, 1985):

Suppose that a UK company buys a hotel in France at a cost of 100 million French francs (FF). The exchange rate at the time was 1 pound = FF10. The UK company contributes 5 million pounds as equity and borrows FF50 million locally (10% interest rate). Net cash flows amount to 20 per cent of its current value each period.

With no inflation in either the UK or France, the income generated in each period is (in millions):

Cash inflow	FF 20
less interest	(FF 5)
Profit	FF 15 = 1.5 pounds (@ 1 pound=FF10)

With no inflation in the UK but a 10% inflation rate in France, and the UK interest rate remaining at 10% but the interest rate in France at 21%, the income generated in each period (again in millions):

Cash inflow	FF 22
less interest	(FF 10.5)
Profit	FF 11.5 = 1.05 pounds (@ 1 pound= FF11)

Assuming that purchasing power parity holds, the apparent decline in the income may be blamed on the distortions introduced into historical cost accounts in times of inflation. Under the temporal method in FAS 8, the hotel is translated at the end of the first period at the historical rate of 1 pound = FF10. But the franc liability is translated at the closing rate of 1 pound = FF11, so its sterling value has fallen from 5 million pounds to 4.55 million pounds. There is thus an exchange difference of 0.45 million pounds to be added to the reported profit of the company, bringing the total profit generated by the activities of the hotel to 1.5 million pounds.

Under the current rate method, both the physical asset and the monetary liability are translated at 1 pound= FF11, so the parent company's net investment in the hotel appears to have declined from 5 million pounds to 4.55 million pounds. This "loss" is not, however, deducted from the 1.05 million pound profit already reported; instead it is taken to reserves.

In this example, it is clear that the temporal method is correcting the "distorted" franc profit and loss account of the hotel, bringing it into line with the "undistorted" UK parent accounts. The current rate method, by contrast, allows any distortions in the currency profit measures to be preserved.

When there is no inflation in France, but the inflation in the UK results in a depreciation of sterling such that 1 pound = FF9, translation of the hotel income statement shows a sterling profit that has increased from 1.5 million pounds as in the no-inflation case to 1.67 million pounds.

Translation under the temporal method results in a deduction of a loss on the franc borrowing of 0.56 million pounds, leaving a net profit of only 1.11 million pounds. The current rate method, on the other hand, takes an exchange gain of 0.56 million pounds to reserves.

In this case it may be seen that the Temporal method is transferring to the hotel accounts a distortion arising in those of the UK parent from conditions of inflation--namely, a failure to take credit for gains arising on liabilities that are fixed in sterling terms.

APPENDIX IV. TAX EFFECTS OF TRANSLATION METHODS

From Nancy L Abbott, "Translation of Long-Term Debt: The Book and Tax Consequences", *International Tax Journal* 5 (February 1979): 227-230.

Example 1: US dollar devaluation.
Local Currency (LC) increases in value from LC1 = $1 to LC1 = $2.

	LC = $1	Tax method (Current-noncurrent)	Financial Reporting method (Temporal)
Current assets	400	800	800
Fixed assets	600	600	600
	1000	1400	1400
Current liabilities	200	400	400
Long-term debt	600	600	1200
Equity	200	400	(200)
	1000	1400	1400

Under both methods, current assets and current liabilities increase according to the change in exchange rate. Long-term debt is a monetary item that remains the same under the current-noncurrent method but increases under the temporal method. For tax purposes, the equity increased by $200, from $200 to $400. For financial reporting purposes, equity decreased by $400 from $200 to -$200. Thus, the $200 increase in equity is taxable under tax rules. Assuming a 46% tax rate, the tax liability is $92. Thus, the decline in the dollar or increase in foreign currency is disadvantageous because a book loss of $400 plus tax on the gain of $92 results in a net after-tax loss of $492.

Example 2: US dollar increases in value.
Local Currency (LC) devalues from LC1 = $1 to LC1 = $.50.

	LC = $1	Tax method (Current-noncurrent)	Financial Reporting method (Temporal)
Current assets	400	200	200
Fixed assets	600	600	600
	1000	800	800
Current liabilities	200	100	100
Long-term debt	600	600	300
Equity	200	100	400
	1000	800	800

For tax purposes, the equity account declines by $100, from $200 to $100, while for financial reporting purposes the equity account increases by $200, from $200 to $400. The net benefit is $246, $200 book gain plus $46 tax saving on the $100 loss, assuming a 46% tax rate.